29TACD2019

BETWEEN/

C.

Appellant

V

REVENUE COMMISSIONERS

Respondent

DETERMINATION

Introduction

This is an appeal against an amended notice of assessment to income tax issued by the Respondent on 20 December 2012, in respect of the tax year of assessment 2007 and against an amended notice of assessment to income tax issued by the Respondent on 21 December 2016, in relation to the tax year of assessment 2011.

The matter in dispute relates to whether payments to the Appellant of €1,076,467.11 and €1,223,526.65 from the two main shareholders in the AB Group (namely XY Capital Partners Global Aggregator LP ('XYCPGALP') and AB Feeder GP Limited 'ABFGP') are subject to income tax as emoluments in accordance with section 112 TCA 1997 or whether the payments comprised a gift from the shareholders to the Appellant, taxable in accordance with the Capital Acquisitions Tax Consolidation Act 2003, as amended ('CATCA2003').

In 2007, the Appellant as Group Chief Executive Officer of the AB Group, was notified of the payments by letter dated 14 June 2007 from XY Partners and by letter dated 29 June 2007 from ABFGP. The June 2007 letters described each payment as a '*gift*'. The payment, totalling approximately €2.3m was made in March 2011 proportional to the respective shareholdings of XYCPGALP and ABFGP at that time.

The Appellant took the view that the sum received was a gift and in September 2011 the Appellant discharged capital acquisitions tax ('CAT') of €596,350 by filing a capital acquisitions tax return (form IT38) for the period 1 September 2010 to 31 August 2011, in respect of the receipt of the sum of €2.3m.

The Respondent contended that the payment was within the charge to tax under Schedule E based on the provisions of section 18(2) Case III(f) of the Taxes Consolidation Act 1997, as amended (hereafter 'TCA 1997'). The basis of assessment of persons chargeable to tax under Schedule E is contained in section 112 TCA 1997.

The Appellant's CAT return was filed prior to the raising of the amended income tax assessments. The Appellant appealed both assessments. Prior to the hearing of this appeal and by case management conference convened in accordance with section 949T TCA 1997, the parties agreed that both appeals would be heard simultaneously.

Background

The Appellant joined the ZA Group in 1998 as Chief Financial Officer. The ZA Group was taken private in 2002 when it was acquired by a private equity fund managed by XY Partners.

Following the take-private of the ZA Group in October 2002, the Appellant became CEO of the group. In late 2005, the ZA Group merged with Company B. From 2005 to 2007 the Appellant was Group CEO of the AB Group ('ABG'). This merger was a success and in 2007 the ABG board took a decision to re-float the combined group by way of Initial Public Offering ('IPO'). In March 2007, ABG was re-floated on the Irish and London Stock Exchanges when approximately €1.5bn of new equity capital was raised. On 9 February 2007, the Appellant was appointed Group Chief Executive Officer of AB plc, having previously served as Group Chief Executive Officer of ABG.

An overview of the work leading up to the IPO in 2007 is summarised in the Annual Report for the year ended 31 December 2007 which is paraphrased as follows;

AB Group has moved towards industry leadership over the past 5 years. Between 2002 and 2005, in difficult market conditions, immense progress was made. Over that period, we sold a substantial amount of non-cash generating assets and spent a substantial amount on acquisitions and disposed of major associates.

In December 2005, ZA Group and Company B merged to become a clear and focussed market leader in Europe with a market share, twice that of our nearest competitor. With operations in

over 30 countries in Europe and Latin America combined, we continue to increase our substantial customer base.

In June 2008, Anglo Irish Bank provided a loan facility of €1.38 million to the Appellant to enable him to purchase €1.2m shares in AB plc. Security for the loan was a first legal charge over the shares purchased and *'an undertaking by the Appellant to remit sufficient proceeds of a gift receivable from XY Capital Partners and AB Feeder GP to repay the facility.'*

In March 2011, the Appellant received payments of €1,076,467.11 and €1,223,526.65 (totalling approximately €2.3m) from XYCPGALP and ABFGP, both shareholders in AB plc, both non-resident entities and both private equity firms. The payments were made based on their respective shareholdings in the AB Group at the time of payment and differed slightly from the amounts referred to in the June 2007 letters. The payments were made in March 2011 at which time XYCPGALP held 15.8% and ABFGP held 18% of the shares in AB plc.

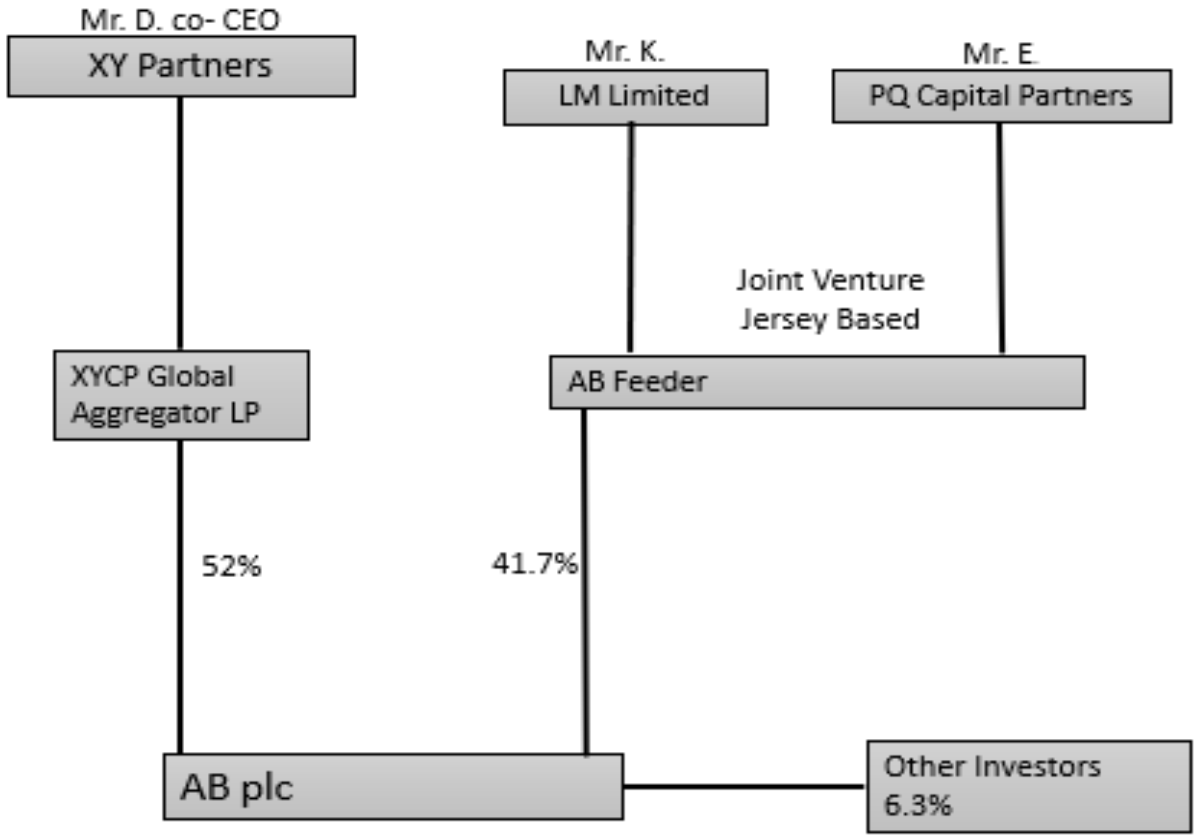
While the Appellant had been informed of the payments by telephone approximately six weeks prior to the June 2007 letters, the Appellant was notified in writing in June 2007 by letter from XY Partners dated 14 June 2007 and by letter from ABFGP dated 29 June 2007. The June 2007 letters described each payment as a '*gift*'.

During the period 2011 through 2013, XYCPGALP and ABFLP disposed of their shareholdings, such that, at the end of this period they no longer held any shares in AB plc.

In his witness statement Mr. D., co-CEO of XY Partners, stated in relation to the ABG shares that '*circa US$450 million was invested and what came out was circa US$800 million.'* A profit of US$350m was made on the investment and from this, a total sum of €5.8m was paid to the four executives including the Appellant, in 2011.

OWNERSHIP STRUCTURE

(prior to the IPO)



Legislation

Section 112 TCA 1997 – Basis of assessment, persons chargeable and extent of charge

(1) Income tax under Schedule E [shall be charged for each year of assessment] on every person having or exercising an office or employment of profit mentioned in that Schedule, or to whom any annuity, pension or stipend chargeable under that Schedule is payable, in respect of all salaries, fees, wages, perquisites or profits whatever therefrom, and shall be computed on the amount of all such salaries, fees, wages, perquisites or profits whatever therefrom for the year of assessment.

(2)(a) In this subsection, "emoluments" means anything assessable to income tax under Schedule E.

Section 18 TCA 1997 – Schedule D

(1) The Schedule referred to as Schedule D is as follows:

SCHEDULE D

1. Tax under this Schedule shall be charged in respect of –

(a) the annual profits or gains arising or accruing to –

(i) any person residing in the State from any kind of property whatever, whether situate in the State or elsewhere,

(ii) any person residing in the State from any trade, profession or employment, whether carried on in the State or elsewhere,

(iii) any person, whether a citizen of Ireland or not, although not resident in the State, from any property whatever in the State, or from any trade, profession or employment exercised in the State, and

(iv) any person, whether a citizen of Ireland or not, although not resident in the State, from the sale of any goods, wares or merchandise manufactured or partly manufactured by such person in the State,

and

(b) all interest of money, annuities and other annual profits or gains not charged under Schedule C or Schedule E, and not specially exempted from tax,

in each case for every one euro of the annual amount of the profits or gains.

2. Profits or gains arising or accruing to any person from an office, employment or pension shall not by virtue of paragraph 1 be chargeable to tax under this Schedule unless they are chargeable to tax under Case III of this Schedule.

(2) Tax under Schedule D shall be charged under the following Cases:

Case I – Tax in respect of –

(a) any trade;

(b) profits or gains arising out of lands, tenements and hereditaments in the case of any of the following concerns –

(i) quarries of stone, slate, limestone or chalk, or quarries or pits of sand, gravel or clay,

(ii) mines of coal, tin, lead, copper, pyrites, iron and other mines, and

(iii) ironworks, gasworks, salt springs or works, alum mines or works, waterworks, streams of water, canals, inland navigations, docks, drains or levels, fishings, rights of markets and fairs, tolls, railways and other ways, bridges, ferries and other concerns of the like nature having profits from or arising out of any lands, tenements or hereditaments;

Case II – Tax in respect of any profession not contained in any other Schedule;

Case III – Tax in respect of –

> *(a) any interest of money, whether yearly or otherwise, or any annuity, or other annual payment, whether such payment is payable in or outside the State, either as a charge on any property of the person paying the same by virtue of any deed or will or otherwise, or as a reservation out of it, or as a personal debt or obligation by virtue of any contract, or whether the same is received and payable half-yearly or at any shorter or more distant periods, but not including any payment chargeable under Case V of Schedule D;*
>
> *(b) all discounts;*
>
> *(c) profits on securities bearing interest payable out of the public revenue other than those charged under Schedule C;*
>
> *(d) interest on any securities issued, or deemed within the meaning of section 36 to be issued, under the authority of the Minister for Finance, in cases where such interest is paid without deduction of tax;*
>
> *(e) income arising from securities outside the State except such income as is charged under Schedule C;*
>
> *[(f) income arising from possessions outside the State except, in the case of income from an office or employment (including any amount which would be chargeable to tax in respect of any sum received or benefit derived from the office or employment if the profits or gains from the office or employment were chargeable to tax under Schedule E), so much of that income as is attributable to the performance in the State of the duties of that office or employment;]*

Case IV – Tax in respect of any annual profits or gains not within any other Case of Schedule D and not charged by virtue of any other Schedule;

Case V – Tax in respect of any rent in respect of any premises or any receipts in respect of any easement;

and subject to and in accordance with the provisions of the Income Tax Acts applicable to those Cases respectively.

(3) This section is without prejudice to any other provision of the Income Tax Acts directing tax to be charged under Schedule D or under one or other of the Cases mentioned in subsection (2), and tax so directed to be charged shall be charged accordingly.

Section 2 CATCA2003 – General interpretation

'gift' means a gift which a person is by this Act deemed to take.

Section 5 CATCA2003 – Gift deemed to be taken

5.(1) For the purposes of this Act, a person is deemed to take a gift, where, under or in consequence of any disposition, a person becomes beneficially entitled in possession, otherwise than on a death, to any benefit (whether or not the person becoming so entitled already has any interest in the property in which such person takes such benefit), otherwise than for full consideration in money or money's worth paid by such person.

Submissions in brief

The submission of the parties can be summarised as follows;

The Appellant submitted that the payment of €2.3m was not an emolument subject to income tax in accordance with section 112 but that the payment was a gift and was liable to capital acquisitions tax ('CAT') which he had discharged. The Appellant submitted that the payment was made to the Appellant in respect of his personal qualities, and for gratitude, appreciation, admiration and friendship and that it formed part of the personal equation and was not taxable as an emolument arising from employment.

The Respondent submitted that the payment of €2.3m satisfied all of the requirements to come within the charge to tax under section 112 TCA 1997. The Respondent submitted that

the Appellant, having led the AB Group through a successful reorganisation followed by a successful IPO, was paid the sum of €2.3m in recognition of the Appellant's significant contribution to the successful re-flotation of the company. The Respondent submitted that the payment arose from the Appellant's role as Group Chief Executive Officer of ABG and that the sum was an emolument assessable to income tax under Schedule E.

EVIDENCE

Documentary Evidence

Documentary evidence furnished in evidence included *inter alia*; letters to the Appellant dated 14 June 2007 and 29 June 2007, board minutes of ABFGP Ltd dated 28 June 2007, the unaudited financial statements for AB Feeder LP for the year ended 31 December 2011, the unaudited financial statements for AB Feeder GP for the year ended 31 December 2011, the Anglo Irish bank loan correspondence, AB Group plc annual report 2007 together with the AB plc IPO prospectus dated March 2007 and the XYCPGALP Limited Partnership agreement.

Excerpts from these documents are cited in the analysis below.

Witness evidence

On behalf of the Appellant, evidence was provided by; Mr. G., consultant in executive compensation, Mr. C., Appellant, Mr. D., co-CEO of XY Partners and Mr. H., Partner with PricewaterhouseCoopers. On behalf of the Respondent, evidence was provided by Mr. J., consultant in corporate finance and capital markets.

The evidence of the witnesses overlapped to an extent as regards factual matters addressed. The evidence is summarised below under the following sub-heads;

a) Notification of the payment
b) Source of the payment
c) Calculation of the payment
d) To whom the payment was made
e) Timing of the payment
f) Adequacy of the Appellant's remuneration
g) The Appellant's work and work ethic
h) Description and classification of the payment in documents

i) The stated and submitted basis for making the payment
j) Accounting standards and reporting

a) Notification of the payment

The Appellant advised that he received a phone call after the IPO in late April/early May 2007 from Mr. D., co-CEO of XY Partners. Mr. D. advised the Appellant that he wanted to make a gift to the executive team in recognition of a great job done for which he was extremely grateful.

By letters dated 14 June 2007 and 29 June 2007, the Appellant received formal notification that payments of €1,076,467 and €1,223,526 would be made by the shareholders (namely, XYCP Global Aggregator LP and AB Feeder GP Ltd) to the Appellant after their shareholdings in AB Group were sold.

The letter dated 14 June 2007 from XY Partners provided;

> ***'Re: Our Investment in ABG***
>
> *Dear Mr. C.,*
>
> *I am writing to express our deep appreciation of your efforts and commitment throughout the period of our investment in AB Group, culminating in the recent, very successful IPO. Everyone at XY Partners is conscious of the sacrifices that you made in this period of your life to deliver the exceptional return that we have achieved to date.*
>
> *In recognition of this and as a concrete expression of our gratitude, we have decided to make a gift to you of €1,075,150. We will, of course, expect that you will comply with all of your obligations as to disclosure and taxation in respect of our gift.*
>
> *We intend on making payment to you shortly after we achieve liquidity in respect of a significant part of our shareholding in AB Group.*
>
> *Yours sincerely*
>
> *Mr. D'*

The letter dated 29 June 2007 from ABFGP Ltd. provided;

> *'Dear Mr. C.*
>
> **AB Feeder L.P. (the "Limited Partnership")**
>
> **Investment in AB Group**
>
> *We are writing to express our deep appreciation of your efforts and commitments through the period of our investment in the AB Group, culminating in the recent, very successful IPO. Everyone at AB Feeder GP Limited is conscious of the sacrifices that you made in this period of your life to deliver the exceptional return that we have achieved to date.*
>
> *In recognition of this and as a concrete expression of our gratitude, we have decided to make a gift to you of €1,224,850. We will, of course, expect that you will comply with all of your obligations as to disclosure and taxation in respect of our gift.*
>
> *We intend on making payment to you shortly after we achieve liquidity in respect of a significant part of our shareholding in AB Group.*
>
> *Yours sincerely*
>
> *For and on behalf of*
>
> ***AB Feeder G.P. Limited***
>
> *As General Partners on behalf of*
>
> ***AB Feeder L.P.'***

The notification of the payment is non-contentious insofar as both parties accepted that formal notification took place by correspondence dated 14 June 2007 and 29 June 2007 and informal notification took place by telephone in late April/early May 2007.

b) Source of the payment

The Appellant stated that the indicated source of the funds for the gift was that when XYCPGALP and ABFGP Ltd. obtained adequate liquidity, they would fund the gift from those funds.

A note of the minutes of a meeting of the directors of AB Feeder GP Ltd. dated 28 June 2007 provides: *"The Chairman reported that the meeting had been convened to consider and, if thought fit, approve IPO bonuses as detailed within the meeting documentation circulated to members of the AB management team in appreciation for their efforts and commitments throughout the period of our investment in the company [culminating] in the recent successful IPO"*

Item 4.4 of the minutes provides; '*The sum of €3.94 million be approved for payment to the recipients, to be settled at the time of a secondary offering from such proceeds, subject to confirmation of company solvency at the time of settlement*.'

As is clear from the letters dated 14 June 2007 and 29 June 2007, the payments of €1,076,467 and €1,223,526 were notified to the Appellant by the shareholders in AB plc., namely, XYCPGALP and ABFGP and those letters stated that*: 'We intend on making payment to you shortly after we achieve liquidity in respect of a significant part of our shareholding in AB Group.'*

These payments were paid to and received by the Appellant in 2011, by the shareholders of AB plc., XYCPGALP and ABFGP Ltd. The payments were not made by the Appellant's employer, AB plc, nor were they made by XY Partners nor were they made by Mr. D. in a personal capacity.

c) Calculation of the payment

Mr. D. gave evidence that the payments made were calculated at twice the respective salaries of each of the recipients namely; the Appellant, Mr. L., Mr. M. and Mr. P.

Senior Counsel for the Respondent asked Mr. D. why the payments were related to salary. Mr. D. replied that '*it seemed about the right amount'.*

During cross-examination of Mr. D., by Senior Counsel for the Respondent, the following exchange occurred on day two of the hearing;

> *'Q: why would it be twice salary? I mean if you are making a gift to somebody why would it be twice their salary?*
>
> *A: It was --- there was no precision to it. It was just one of those things, it seemed about the right amount.*
>
> *Q: Okay. But there was precision to it, with respect, now, Mr. D., because it does translate precisely to twice the 2006 salary of each of the four individuals concerned, so it was quite precise?*
>
> *A: But it could have been one times, it could have been three times. Two, I am saying it was …*
>
> *Q: I suppose the question I need to ask you is this, Mr. D.: If it was a gift why does it have to be related to salary?*
>
> *A: It just gave us a marker, that's all.*
>
> *Q: But if you are making a gift to somebody you could come up with any amount?*
>
> *A: I suppose what we were looking to do was to try to make a significant statement of our gratitude and our appreciation. I mean two times salary seemed like a significant statement.*
>
> *Q: So –*
>
> *A: It could have been, you know maybe someone's interpretation would be one times would be significant or three times. We thought twice was significant.*
>
> *Q: And it was related to salary?*
>
> *A: It was two times his salary.'*

Thus, it is not disputed that the payments made were calculated at twice the respective salaries of each of the four recipients.

d) To whom the payment was made

The three other members of the senior executive team received payments from the shareholders of AB plc. similar to the Appellant with a sum of approximately €5.8m paid in total to the four executives. Mr. D. gave evidence that the payments made were calculated at twice the respective salaries of each of the four recipients namely; the Appellant, Mr. L, Mr. M. and Mr. P.

e) Timing of the payment

Mr. D. stated that the global crash in 2008 delayed the sale of the shareholdings as the shares could not be disposed of until the share price recovered in 2011. Thus, the shareholders began disposing of their shareholdings in 2011. The final tranche of shares was sold in 2012.

A profit of $350m was made on the investment and from this, the payment of €5.8m was paid to the four executives including the Appellant, in 2011.

f) Adequacy of the Appellant's remuneration

Mr. G., a consultant in the field of executive compensation was asked by the Appellant to assess the remuneration of the Appellant over the period 2002 to 2007. Mr. G. gave evidence on behalf of the Appellant, in an expert capacity.

Mr. G. stated that in addition to remuneration, the Appellant received approximately €10m of value through long-term incentives. He stated that, adding the value of the Appellant's long-term incentives to the Appellant's other remuneration on a straight annualised basis, provided an average remuneration during the period the business was in private hands, of over €4m per annum. Mr. G. stated that the Appellant '*has therefore been very well remunerated*.'.

A witness statement prepared on behalf of Mr. G. and signed by him, was read into evidence. At paragraphs 20 -22 of his witness statement, Mr. G. stated;

> *'My experience of* [Private Equity] *organisations is that they can offer generous remuneration packages but that they are quite 'hard' in expecting delivery of performance. Rewards are provided in line with contractual expectations only.*

> *The remuneration package offered to Mr. C. is consistent with the remuneration package I would expect to see.*
>
> *I have been asked to consider if I have any experience or knowledge of* [Private Equity] *organisations making gifts or non-contractual payments to executives. It is my experience that this would be extremely unusual. Indeed, I have never come across an example or heard of an example where a* [Private Equity] *organisation has made such a payment. It would also seem inconsistent with the cultural approach of* [Private Equity] *organisations.'*

The rarity of these types of payments was echoed by Mr. J. in his expert report where he stated; *'I comment that in my experience the making of gifts is not a normal part of corporate culture. … Thus, if Mr. C. and the other members of the senior management team had not provided any services to the A group, it would defy commercial logic or market practice, for the company, or its shareholders, to make payments to these individuals.'*

Mr. J., in his expert report [quoting Leslie and Lyle (2009) 'Managerial Incentives and Value Creation, Evidence from Private Equity'] cited the phrase: *'… private equity firms buy companies, fix them, and then sell them'.*

He stated that the making of gifts was not a normal part of corporate culture and that if the Appellant and the other members of the senior management team had not provided any services to the A group, it would defy commercial logic or market practice for the company or its shareholders to make payments to these individuals.

Mr. G., expert witness on behalf of the Appellant, concluded that the Appellant was very well remunerated for his work. Mr. G. stated '*I have provided the analysis on the basis that, if an individual was underpaid against the benchmark data and then subsequently received a payment, it could be argued that such payment could be considered as deferred remuneration. However, in this case the incumbent was substantially rewarded already and I would therefore consider that this argument does not apply*.'

An analysis of the Appellant's remuneration confirmed that in 2002 the Appellant's bonus and deferred bonus added together exceeded his annual salary. In 2003, his bonus exceeded his annual salary. In 2004 it was less than annual salary. In 2005 and 2006 it was 100% of annual salary and in 2007 it was 70% of annual salary. These figures are contained in Mr. Gs' witness statement.

In the Appellant's witness statement, he stated; *'Had the PE's not decided to give the top team a very generous gift well after the successful IPO (and of their own volition), because of the compensation package we enjoyed, we would have had no basis whatsoever for being unhappy with the company's treatment and compensation of both me and the team.'*

The Appellant continued*; '….. In my own case, my base salary and total package was well up at the upper end of comparator groups, as evidenced by benchmarking done for the board remuneration committee and many public comparisons run by newspapers and business magazines.'*

In oral evidence he stated; *'To be honest with you, I always felt I was extremely well paid and well rewarded …. I've never had a particular problem with my remuneration in the plc world. But it certainly, in comparative terms, has been always well up there relative to the peer group…'*

In conclusion on this point, the evidence, including expert evidence, reflected that the Appellant was adequately remunerated for his work and the Appellant himself accepted that this was the case.

g) The Appellant's work and work ethic

The Appellant worked long hours and the Appellant, in his witness statement stated; *'In summary, the success of the IPO in 2007 depended on a significant amount of work over a number of years leading up to it including acquisitions, integration efforts, disposals, cost rationalisation programmes (including plant closures, headcount reduction etc.) major refinancing initiatives and a myriad of other activities involving significant travel, absence from home and long hours of work.'*

An overview of the changes which took place in the period leading up to the IPO in 2007 was summarised in the annual report for the year ended 31 December 2007, which is paraphrased as follows;

> *AB Group has moved towards industry leadership over the past 5 years. Between 2002 and 2005, in difficult market conditions, immense progress was made. Over that period, we sold a substantial amount of non-cash generating assets and spent a substantial amount on acquisitions and disposed of major associates.*

> *In December 2005, ZA Group and Company B merged to become a clear and focussed market leader in Europe with a market share, twice that of our nearest competitor. With operations in over 30 countries in Europe and Latin America combined, we continue to increase our substantial customer base.*

The IPO prospectus published in March 2007, details the enormous amount of work undertaken. The final paragraph, encapsulates a concise statement of what was involved, which his paraphrased as follows; *Management has implemented a wide range of strategic reforms in the operations of the Group, has influenced changes in the industry and has engaged in closure decisions and retention decisions across teams in over 30 countries.*

At paragraphs 25 and 26 of his witness statement the Appellant, stated;

> *'We had come through some very tough times together involving punishing hours and Mr. D. had this very much in mind when making the gift. Mr. D. was very close to us and knew every hour the team worked. At the time of the merger in 2005 I worked non-stop for about 7 months. When I was working on Saturdays and Sundays, Mr. D. would regularly ring me out of solidarity. I remember that during the merger discussions with Company B, I went to Hawaii with the whole family on a holiday that had been planned a long time previously. It was to celebrate my wife's birthday. As a result of it being during merger discussions, I arranged to have a separate room which served as my office with computers/printers etc. so that I could work European times. Most of this holiday was given over to the merger discussions. As with the IPO speed was of the essence in the merger discussions and the maintenance of energy and dynamic behind the process was (and is) ABG's style – this always involves long hours and weekend working in order to stay ahead of the agenda and maintain control of the dynamic. The period from 2002 to 2007 was typified by such circumstances, and Mr. D./XYP (and laterally AB Feeder) knew it. During this period, it was not at all uncommon to arrive home on a Saturday morning, work in the office for the rest of Saturday and Sunday morning and then fly out again on Sunday afternoon. As a consequence, I missed many family events and my first grandchild was two days old before I got to see her as I was in Latin America when she was born.*
>
> *Most private equity firms do not care about personal sacrifice - XYP are different – I believe Mr. D. was conscious of the great dedication and commitment that I and my colleagues had made over many years.'*

The June 2007 letters spoke of *'... the sacrifices that* [the Appellant] *made in this period of* [his] *life to deliver the exceptional return that we have achieved to date.'* During re-examination of Mr. D. by QC for the Appellant, Mr. D. was asked what he meant by the reference to '*sacrifices'* in the letter and Mr. D. responded;

> *'.. what I am referring to there is what I mentioned earlier which is in my 36 years in this business I have never seen a chief executive officer work as hard as Mr. C. with as much commitment… My partners at XY were aware of that. You know Mr. C. works…, worked non-stop, weekends, you name it, he was working. It was beyond anything I had ever seen. It was beyond anything that Mr. E. or Mr. K. had ever seen. It was extraordinary, it was extraordinary. It was incredible leadership for the organisation and it's really that extraordinary leadership that we felt grateful for. That's what I am getting at in that letter.'*

Mr. J., in his expert report stated; '*Overall it would be my view, and I think an uncontroversial one, that Mr. C. played a pivotal role in developing the A group whilst it was in private ownership (2002-2007), and in taking the group, through the IPO process and beyond.'*

Mr. D. in evidence stated; '*I spoke to the other private equity investors in ABG….They also recognised that the IPO would not have been possible without Mr. C. and his team*'. He continued; '*Mr. E., who represented PQ and Mr. K., who represented LM on ABG board were very supportive of the decision taken by XYP to make a gift….They both saw the extra work and effort that had been put in, particularly between 2005 and 2007. They knew that the IPO could not have happened without this. They were really appreciative and wanted to be part of a gesture that expressed their gratitude*".

And further; '*There was no way that this was intended to be an incentive for the future or any way linked to the future. We had made a commitment irrespective of performance. …… It was not in any way forward looking, but it was a recognition of Mr. C.'s sacrifice, my admiration and our friendship*".

Mr. D. in evidence, emphasised the rarity of payments of this nature, stating that he could remember only one occasion where something comparable happened and that was in 1987 when the CEO of a successful company in which XYCPGALP had invested was given a car as a token of appreciation.

It is clear from the evidence that payments of this nature were extremely rare. It was unusual for an employee in this field to be rewarded financially outside of their contractually agreed remuneration, and in particular to be rewarded so significantly.

It is clear from the evidence that the Appellant worked diligently and committedly for ABG, was devoted in terms of his work, gave enormously of his time and made personal sacrifices.

In 2007, the culmination of the Appellant's work resulted in a successful IPO which achieved exemplary level returns for shareholders and investors.

h) Description and classification of the payment in documents

Many documents were opened in the course of the hearing, and references to the payment received by the Appellant and his colleagues, as set out in those documents, were debated and considered as follows;

The Appellant contended that the June 2007 letters were strong evidence of motivation by the donor, as the letters expressed '*deep appreciation*' '*gratitude*' and also used the word '*gift*'.

The Respondent regarded the letters as evidence that the payments were received by the Appellant for the work carried out in relation to the IPO and in this regard relied on references to '*your efforts and commitments through the period of our investment in the AB Group, culminating in the recent, very successful IPO*' and to the reference to '*the sacrifices that you made in this period of your life to deliver the exceptional return..'.*

The minutes of a meeting of the directors of ABFGP which took place on 28 June 2007 in Jersey, provide:

> *'The Chairman reported that the meeting had been convened to consider and, if thought fit, approve IPO bonuses as detailed within the meeting documentation circulated to members of the AB management team in appreciation for their efforts and commitments throughout the period of our investment in the company [culminating] in the recent successful IPO'*

Item 4.4 of the minutes provides as follows;

> "*The sum of €3.94 million be approved for payment to the recipients, to be settled at the time of a secondary offering from such proceeds, subject to confirmation of company solvency at the time of settlement*."

Senior Counsel for the Respondent opened the unaudited financial statements for ABFGP Ltd. for the year ended 2011 which referred to the payment to the Appellant and his co-executives as a '*deferred management IPO bonus'*.

Senior counsel also highlighted that in the limited partner's accounts there is mention of a "*decrease in creditors of €3,090,735*", which is a reference to the deferred management bonus. He put to the Appellant in cross-examination that "*if it is a gift, I'd have to suggest to you there is in fact no liability to make a payment of a gift".*

The 2007 annual report of the AB Group plc addresses this which is paraphrased as follows:

> *In June 2007, a cash amount of approximately €5.8 million was awarded to the executive Directors (€5.3million) and the Company Secretary by the major shareholders XY Capital Partners and AB Feeder GP Limited and is payable directly by those shareholders. The award was made in connection with the successful flotation of the Company.*

On behalf of the Respondent, it was pointed out that the language used under the heading '*Related Party Transactions'*; in the 2007 annual report referred to *'compensation of key management personnel'*.

The Appellant stated in evidence that: *'My start point was that I was amazed that we were considering and required to report this in this fashion in this note, given that my starting point is, was and will be that it was a gift… However, for technical Companies Act and accounting and reporting reasons, I was advised by our technical advisors, in conjunction with our finance people, that this needed to be reported. And if that was the case then obviously I complied.'*

As regards the loan from Anglo Irish bank, the Appellant's witness statement, at paragraph 34, provided: *"I included the gifts as security in the Loan Agreement dated 27th May 2010 between me and Anglo Irish Bank…The effect of this was that the amount I expected to receive by way of the gift would be available to repay my debts in the event of default. I included this as*

security to ensure that I had sufficient cover with Anglo Irish Bank to encourage them not to call in the loans which would have created problems for me."

During cross-examination, Senior Counsel for the Respondent stated that; *'.. the point I have to make to you is that unless you had certainty that that payment was made, unless it was a legally enforceable obligation, that security would be worth nothing to Anglo Irish Bank.'*

The Appellant responded by stating that the shares in the company had devalued at that stage and so the payment was the main security for the Anglo Irish loan. The Respondent emphasised the fact that Anglo Irish Bank was prepared to make the loan on that basis. In response, QC for the Appellant pointed to the fact that Anglo Irish Bank were aware that the payment was a gift as the word '*gift*' was used in the 2010 loan agreement security documentation

Mr. J., expert witness, in his report provided his opinion that; *'I also comment that this was not a singular award of €2.3m to Mr. C., but rather it was one of four similar payments (totalling €5.8m), made to Mr. C. and the other three members of the senior management team. I give my view that in a financial sense I would regard these payments simply as bonuses (albeit deferred bonuses) for the work undertaken by the senior management team during the period of private ownership, including the work needed to take the group through a successful IPO.'*

Mr. J. in his expert report stated his opinion as follows; *'That the awards were made, and borne by, the private equity funds, rather than AB plc, is indicative of the awards being for the period leading up to the IPO (when the company was owned by the private equity funds), rather than the period after the IPO when it was owned by a mix of private equity funds and other, new, shareholders (albeit with the private equity funds owning a major portion of the company's share capital, until share disposals started to take place in 2011). Also, that the awards were not paid over until 2011, when the private equity funds realised their first tranche of income from selling their shares in AB plc, seems to me entirely consistent with the industry norm under which private equity houses seek to align management compensation with the returns that they (the private equity funds) receive.'*

Mr. J. also stated, at paragraph 112 of his expert report that in his opinion; *'That the awards to the other three members of the senior management team were made following consultation between Mr. C. (as CEO and leader of the senior management team) and XY LLC would .... also be consistent with a bonus award and allocation process.'*

Mr. G. in evidence stated that it would be extremely unusual for private equity organisations to make gifts or non-contractual payments to executives. He also stated that it would be *"inconsistent with the cultural approach of private equity organisations*" to make payments of this nature.

Mr McDonald put it to Mr. G. that private equity firms *can* issue discretionary bonuses. Mr. G. stated that private equity companies are not restricted by law from issuing discretionary bonuses but that rewards are usually paid out subject to predetermined performance criteria.

Mr. D. in evidence accepted that the payment of a '*gift'* of this nature was extremely rare. Mr. G. and Mr. J. agreed during evidence that the payment of a '*gift'* on this scale was highly unusual.

The Respondent's submission was that the tax classification of the payment as a '*gift'* was inconsistent with the contemporaneous documents including the June 2007 letters, the accounts and the IPO prospectus. The Appellant, cited the June 2007 letters in support of his position that the payment was a gift and relied on corporate and accounting compliance obligations to explain the manner of reporting of the payment in the accounts. QC for the Appellant submitted that the substance of the payment was that it was a gift and contended for a determination based on the substance of the payment, as opposed to the form in which the payment was expressed in company documentation as *'compensation of key management personnel'* or as '*IPO bonus'.*

i) <u>The stated and submitted basis for making the payment</u>

The Appellant stated that he had developed a personal relationship and friendship with Mr. D., having worked closely with him over a period of 6 years leading up to the IPO.

In his witness statement, the Appellant stated; *'Most private equity firms do not care about personal sacrifice – XYP are different – I believe Mr. D. was conscious of the great dedication and commitment that I and my colleagues had made over many years. Given our work ethic there was solidarity between Mr. D. and me. I had no expectations that a gift would be made. If the gift had never been made I would have been perfectly happy, not expecting the gift in the first instance.'*

In addition, the Appellant stated; *'I have always viewed the payments made as a gift. They were an expression of generosity. They were unexpected and motivated by gratitude. It seemed to me consistent with this that they be treated as such for tax purposes as I was advised to do.'*

The Appellant, at paragraph 40 of his witness statement, stated *'By any measure, in my book a conscientious Mr. D. owed me nothing and the gift was and is a measure of his generosity of spirit.*'

The Appellant submitted that there was no legal obligation to pay the money and no contractual entitlement to have it paid and that it was paid out of generosity.

Mr. D. described his relationship with the four members of the management team at ABG which included the Appellant, as one of '*close partners or comrades'.* He stated: "*For Mr. C., I have a high degree of respect, admiration and warmth*. *We have, since we have known each other, seen each other outside work and still do to this day, even though XYP sold its stake in ABG. This is one of those rare cases where a close relationship has been formed and has remained.'.*

He continued; "*The background to this gift is the admiration which I felt in respect of Mr. C. and the rest of the team for their immense dedication and commitment. This was something extraordinary and very rare*".

Mr. D., referring to the payment received by the Appellant, on the second day of hearing stated; *'…it was intended to demonstrate respect and appreciation for the hard work and dedication shown'*.

Mr. D. continued*; 'It was recognition of Mr. C.'s sacrifice, my admiration and our friendship*".

In evidence he stated: '*I spoke to the other private equity investors in ABG….They also recognised that the IPO would not have been possible without Mr. C. and his team ……. Mr. E., who represented PQ and Mr. K., who represented LM on ABG board were very supportive of the decision taken by XYP to make a gift…. They both saw the extra work and effort that had been put in, particularly between 2005 and 2007. They knew that the IPO could not have happened without this. They were really appreciative and wanted to be part of a gesture that expressed their gratitude*'.

In direct examination, Mr. D. was asked; *'Was the amount of the gift dependent on your profit on the disposal of your ultimate exit?'* to which Mr. D. responded; *'No, it had nothing to do with our profit on the disposal, it had nothing to do with that at all. It was purely an expression of gratitude, of admiration, of appreciation for incredibly hard work and dedication over the life of our investment and culminating in the IPO, to getting it done.'*

The Respondent emphasised that the payments were not made personally by Mr. D., but were made collectively by the investors in AB plc.

Senior Counsel for the Respondent stated that the fact that Mr. D. was not paying the money personally meant that friendship and admiration were irrelevant as the investors, i.e. the limited partners, did not have any friendship with the Appellant. Furthermore, the Respondent submitted that money paid for admiration and friendship would not constitute '*partnership expenses'* and would not fall within the conduct of partnership business and in this regard, Senior Counsel for the Respondent opened relevant provisions of the XYCP Global Aggregator Limited Partnership agreement.

Mr. J., on page 31 of his report, stated;

> *'That the rewards were made by shareholders in AB as opposed to AB itself would also indicate that the rewards related to the period leading up to the IPO when the company was owned by the private equity funds rather than the period after the IPO when it was owned by a mix of private equity funds and other new shareholders. Having said that, however, the private equity funds would have a significant interest in the continuing role and performance of Mr. C. and other members of the senior management team given that the private equity funds would be major shareholders in AB plc going forward, holding something like 60% of the group share capital up until the point when they began to sell down their respective shareholdings.'*

Mr. D. stated in evidence on day two of the hearing that there was no relationship between the return to the shareholders and the payment made to the Appellant and his colleagues, however, Mr. D., in paragraph 23 of this witness statement stated; *'It was easier operationally to pay the amount out of the proceeds of the sale of the ABG shares. The amount of 5.8 million needs to be viewed in the context of overall result where circa US$450 million was invested and what came out was circa US$800 million.'*

On day two of the hearing, with Mr. D. under cross-examination by Senior Counsel for the Appellant, the following exchange occurred;

> *'Q: But, Mr. D., I have to suggest to you it makes no sense to make a payment of €5.8 million gratuitously?*
>
> *A: Well, I take issue with that. In our business your reputation is the most important thing that you have.*
>
> *Q: Mm hmm.*
>
> *A: We try to approach the world in a way where we are doing the right thing, regardless of what our obligations might be. We enjoy a reputation for fair dealing, for good partnership. And you may say that that has no value, but I can tell you that it has a lot of value in our world. It has a lot of value when it comes to trying to convince companies and CEOs that they would work with us and not somebody else. Your reputation and how you have treated people in the past is incredibly important. And so to do the right thing, you may say it doesn't make economic sense, but it makes a lot of business sense.'*

In summary, on behalf of the Appellant it was submitted that the payment of €2.3m was made out of gratitude, generosity, respect and appreciation for hard work and dedication shown by the Appellant.

j) Accounting standards and reporting

Mr. H., PwC was the lead partner on the audit of AB plc for the year ended 31 December 2007 and Mr. H. signed the audit opinion in relation to the financial statements in respect of that year. Mr. H. was called to give evidence on behalf of the Appellant as to his understanding of the facts from an accountancy perspective.

> Mr. H. stated that it was appropriate to disclose in the accounts, the payment of €5.8m to the executive directors and company secretary of ABG. The disclosure provided (paraphrased); *In June 2007, a cash amount of approximately €5.8 million was awarded to the executive Directors (€5.3million) and the Company Secretary by the major shareholders XY Capital Partners and AB Feeder GP Limited and is payable*

directly by those shareholders. The award was made in connection with the successful flotation of the Company.

Mr H. in his witness statement, stated that Section 191 of the Companies Act 1963 outlined Irish company law disclosure requirements in respect of directors' emoluments. The Act provides that the emoluments to be included shall include: ".. *any emoluments paid to or receivable by any person in respect of his services as director of the company or in respect of his services while director of the company, as a director of a subsidiary thereof, or otherwise in connection with the management of the affairs of the company or any subsidiary thereof.'*

The section continues*;* '*For the purpose of this section emoluments includes fees and percentages, any sums paid by way of expenses allowances insofar as those sums are charged to income tax, any contribution paid in respect of him under any pension scheme and the estimated money value of any other benefits received by him otherwise than in cash insofar as the sums are charged to income tax*'.

Mr H. stated that '*It was considered by management and the directors that section 191 probably applied since the test appears to encompass any payment made in connection with the management of the affairs of the company and this was very wide. The definition of 'emoluments' was not exhaustive and the view taken was that it would probably apply to a payment of money.'*

Mr. H. also discussed IAS 24 and rule 6.8.8 of the listing rules of the Irish Stock Exchange in the context of the payment received by the Appellant and his executive director colleagues. Mr. H.'s evidence in this regard was that neither IAS 24 nor rule 6.8.8 applied.

In evidence, Mr. H. discussed the accounting treatment of the payment. He referred to note 8 of the 2011 accounts of AB Feeder LP where the payment to the Appellant and his executive director colleagues was treated as a liability. QC for the Appellant asked Mr H. if the note implied any legal obligation to pay. Mr H. replied that liabilities can be caused by two things; a legal obligation or a constructive obligation. He stated that a constructive obligation is where a company takes on certain responsibilities which it proposes to discharge. He stated that one may have liabilities in financial statements which are not legal obligations but which are constructive obligations, and that the tenet of accounting is that both are recorded as liabilities.

QC for the Appellant suggested that the treatment of the payment in the accounts as a liability was not indicative of an obligation to make the payment on behalf of the shareholders and this proposition was accepted by Mr. H..

In conclusion on this point, I am not persuaded that the accounting treatment of the payment provides assistance in ascertaining the nature of the payment for tax purposes. Whether or not the payment falls within IAS 24 or within the Stock Exchange listing rules, or whether or not it falls within Section 191 CA 1963 is not in issue in this appeal. What is in issue is whether the payment falls within Schedule E or whether the payment falls to be taxed as a gift in accordance with the Capital Acquisitions Tax Consolidation Act 2003.

Summary of the evidence

a) Notification of the payment

The notification of the payment is non-contentious insofar as both parties accepted that formal notification took place by correspondence dated 14 June 2007 and 29 June 2007 and informal notification took place by telephone in late April/early May 2007.

b) Source of the payment

As is clear from the letters dated 14 June 2007 and 29 June 2007, the payments of €1,076,467 and €1,223,526 were notified to the Appellant by the shareholders in AB plc., namely, XYCPGALP and ABFGP and those letters stated that*: 'We intend on making payment to you shortly after we achieve liquidity in respect of a significant part of our shareholding in AB Group.'*

These payments were paid to and received by the Appellant in 2011, by the shareholders of AB plc., XYCPGALP and ABFGP Ltd. The payments were not made by the Appellant's employer, AB plc, nor were they made by XY Partners nor were they made by Mr. D. in a personal capacity.

c) Calculation of the payment

It is not disputed that the payments made were calculated at twice the respective salaries of each of the four recipients.

d) To whom the payment was made

The recipients of the payments (of approximately €5.8m in total) were the four members of the senior executive team at ABG namely; the Appellant, Mr. L., Mr. M. and Mr. P.

The payment made to the Appellant was not unique, as all four executives on the senior management team (including the Appellant) were awarded in proportionately the same way, each receiving a sum of twice their salaries.

e) Timing of the payment

The payments were made in 2011 after the sale of the ABG shares and from the proceeds of the sale of those shares.

f) Adequacy of the Appellant's remuneration

The evidence including expert evidence, reflected that the Appellant was adequately remunerated for his work and the Appellant himself accepted that this was the case.

g) The Appellant's work and work ethic

It is clear from the evidence that the Appellant worked diligently and committedly for ABG, was devoted in terms of his work, gave enormously of his time and made personal sacrifices.

In 2007, the culmination of the Appellant's work resulted in a successful IPO which achieved exemplary level returns for shareholders and investors.

h) Description and classification of the payment in documents

Descriptions of the payment varied from '*gift*' in some instances to *'deferred management IPO bonus'* in others. The descriptions in the accounts, in the IPO prospectus, in the annual reports and in correspondence are not in themselves determinative, but constitute items to be considered in the overall analysis, in pursuance of the answer to the question of law arising. The question arising is whether the payment is properly taxable as a gift or alternatively, whether it is taxable as emoluments arising from employment.

As stated below, descriptions and labels given to the payment are not determinative of the character of the payment. In the Irish Supreme Court case of *Wing v O'Connell* [1926] IR 84,

the payment was taxed as an emolument notwithstanding the fact that the payment was described as a '*present*'.

i) <u>The stated and submitted basis for making the payment</u>

In evidence, Mr. D. stated that the payment was made for reasons of '*friendship*' '*admiration*' and 'in *recognition of Mr. C.'s sacrifice'.* He stated; *'... it was intended to demonstrate respect and appreciation for the hard work and dedication shown*' and that *'The background to this gift is the admiration which I felt in respect of Mr. C. and the rest of the team for their immense dedication and commitment.'*

The Appellant stated: *'...Mr. D. owed me nothing and the gift was and is a measure of his generosity of spirit.'*

The June 2007 notification letters referred to the '*deep appreciation'* and '*gratitude*' of the payors and also described the payments as a '*gift*'.

In summary, on behalf of the Appellant it was submitted that the payment of €2.3m was made out of generosity, respect and appreciation for hard work and dedication shown by the Appellant and for gratitude, admiration and friendship.

The relevance of the qualities of friendship, admiration and gratitude etc. are matters to be considered in the overall analysis in pursuance of the answer to the question of law arising, namely; whether the payment is properly taxable as a gift, or whether the payment is taxable as emoluments arising from employment.

j) <u>Accounting standards and reporting</u>

In conclusion on this point, I am not persuaded that the accounting treatment of the payment provides assistance in ascertaining the nature of the payment for tax purposes. Whether or not the payment falls within IAS 24 or within the Stock Exchange listing rules, or whether or not it falls within Section 191 CA 1963 is not in issue in this appeal. What is in issue is whether the payment falls within Schedule E or whether the payment falls to be taxed as a gift in accordance with the Capital Acquisitions Tax Consolidation Act 2003.

ANALYSIS

Wing v O'Connell – legal principles

The Irish Supreme Court case of *Wing v O'Connell* [1926] IR 84 is binding Supreme Court authority and unless set aside by another decision of the Supreme Court under the principles in *Mogul of Ireland Limited v Tipperary (North Riding) County Council* [1976] IR 260, it remains binding authority.

In *Mogul of Ireland*, the Supreme Court of 1975 refused to depart from a judgment of the Supreme Court of 1948 as the applicants to the case before them had failed to establish that the previous Supreme Court decision was clearly wrong. In *Mogul*, Henchy J. stated;

> *'A decision of the full Supreme Court (be it the pre-1961 or the post-1961 Court), given in a fully-argued case and on a consideration of all the relevant materials, should not normally be overruled merely because a later Court inclines to a different conclusion. Of course, if possible, error should not be reinforced by repetition or affirmation, and the desirability of achieving certainty, stability, and predictability should yield to the demands of justice. However, a balance has to be struck between rigidity and vacillation, and to achieve that balance the later Court must, at the least, be clearly of opinion that the earlier decision was erroneous.'*

The facts of *Wing v O'Connell* were as follows; Mr. Wing earned his livelihood as a jockey. His emoluments, consisting mainly of fees receivable, were regulated by a scale set by the Turf Club and varied according to success and the value of the stake. When a jockey was engaged to ride a horse, his engagement ended on the completion of the race. In this instance however, Mr. Wing, having won the race, received a '*present*' of £400 from Colonel Charteris. The letter enclosing the cheque of £400, drawn and signed Colonel Charteris, provided;

'Dear Sir,

Please accept the enclosed present, with my very best thanks, for your very fine riding of Ballyheron in the Irish Derby. It was a very fine performance, and did you the greatest credit. I hope you will soon ride him again to victory.

Believe me,

Faithfully yours,

Richard B Charteris'

The question for consideration was whether the payment was an emolument which arose from Mr. Wing's vocation as a jockey and was thereby subject to income tax within the requisite provisions of the Income Tax Act 2018. The Supreme Court found that the payment was an emolument and was subject to income tax accordingly.

The legal principles that arise from *Wing v O'Connell* may be summarised as follows;

1) Payment in excess of salary - the fact that an employee has been paid fully for his/her work does not have the effect of taking an additional payment, received by the employee, outside the scope of the income tax statute
2) The personal equation - where an employee receives a payment in recognition of the work that he or she has done or the success that he or she has achieved in the work that he or she has done, this is not a basis upon which to suggest that the payment was purely personal and that the payment does not arise from the employment
3) Contractual obligation and voluntariness - there does not need to be a contractual obligation to make the payment in order for the payment to be taxable as income arising from employment. A payment may be voluntary and be taxable as an emolument.
4) Expectation - a payment may be unexpected and be taxable as an emolument.
5) Exceptionality - the fact that a payment may be extraordinary or a one-off does not take the payment outside the scope of the income tax statute.

An application of those legal principles, in the context of the within appeal is set out as follows;

1) Payment in excess of salary

The case of *Wing v O'Connell* proceeded on the basis that Mr. Wing had been fully remunerated for riding the race by the payment to him of professional fees and charges as a jockey and that the £400 sum was paid in addition to his professional fees. On page 99 of the Judgment, Kennedy C.J. stated;

> *'Here let me say that I have no doubt but that Mr Justice Hanna is in error in supposing that Mr Wing received no other emoluments or fees in respect of the particular race, and that the sum of £400 was an inclusive payment covering fees and something over and above in the nature of a gift. I think it is clear from the case as stated that in the ordinary course Mr Wing's fees for riding the race were fixed by the Turf Club, and credited to him in their books and subsequently paid. I propose, therefore, to assume, for the purpose of this judgment, that the sum of £400 was paid in addition to Mr Wing's ordinary professional fees and charges as a jockey under the Turf Club regulations for riding the race.'*

The Court held that the payment of £400 was taxable as an emolument which arose or accrued to Mr. Wing by reason of his vocation as a jockey.

The Appellant in this appeal contended that the payment he received was not made in return for the performance of services as he was adequately remunerated in respect of those services. The Appellant contended that the payment was a bounteous gesture arising, not from the employment, but by reason of qualities personal to him.

In the within appeal, the evidence, including expert evidence, reflected that the Appellant was adequately remunerated for his work and the Appellant himself accepted that this was the case. The submission by the Appellant that the payment of €2.3m received by him did not form part of his remuneration on the basis that there was no deficit in his remuneration is unpersuasive. In *Wing v O'Connell*, the fact that the payment made to Mr. Wing was additional to his remuneration, did not prohibit the characterisation of the payment as an emolument arising from his vocation.

Thus, the adequacy of the Appellant's remuneration is not determinative of the character of the payment made and does not preclude a finding that a payment constitutes a taxable emolument.

2) The personal equation

A payment is not assessable to tax as an emolument if it is made for purely personal reasons i.e. if it forms part of the '*personal equation'*. The '*personal equation'* is described concisely by Maguire on *Irish Income tax 2018* as '*a payment made on purely personal, compassionate or altruistic grounds.'*

In *Wing v O'Connell*, on page 102 of the report Kennedy C.J. stated;

> *'Now, the sum in question was either a profit of Mr Wing's vocation or it was a mere gift or present, not a subject-matter of taxation.*
>
> *By "a mere present" I mean something given without consideration, something not earned by professional services, something not paid for on Mr Wing's part by professional work.'*

The Appellant in the within appeal submitted that *'... in exceptional cases, working as an employee generates recognition, gratitude or a sense of moral obligation, and where this leads to a receipt, that receipt is not one of remuneration but something else…. In those exceptional cases, that something else is not taxable because the operative cause, or reason behind the payment, is not the employment but the recognition, gratitude or sense of moral obligation.'*

In *Wing v O'Connell*, counsel for Mr. Wing, ('Mr. Leonard') made a similar submission insofar as he sought to separate the individual from the professional. At page 102, Kennedy C.J. described this submission as follows;

> *'Mr Leonard has argued that the "personal equation," as he puts it, is the decisive matter between these two alternatives; that, if the personal equation predominates, if the payment was made to him as an individual rather than as a jockey, because of his individual excellence rather than because of the particular exercise of his vocation, even though that excellence is manifested by the professional occasion, then it is not a professional profit, but a mere present—truly a tenuous metaphysical notion to educe from a very material statute. Mr Leonard's own words were, that Wing received the money "not because he was a jockey, but because he was a good jockey," that is to say, because of his excellence, not because of his jockeyship, though Mr Leonard means excellence in jockeyship, thus making a much finer point…'*

While Kennedy C.J. accepted that the '*personal equation'* may arise in certain circumstances, he cited some examples of the circumstances in which it might arise when he continued as follows;

> *'Granting, however, as in my opinion it may be granted, that a payment or present to a professional man, even in the course of the exercise of his vocation, is not a profit or gain of the profession or vocation for the purpose of Case II of Schedule D, if it be a mere gift or present to him as an individual, the personal equation predominating, and does not arise or accrue from the profession or employment, I turn to the facts in this case as stated by the special Commissioners. I cannot, however, find in the case a fact or a trace of positive evidence of the purely personal reasons, the predominating "personal equation," which would stamp this payment with the character of a mere gift or present, and prevent it from being reckoned as a professional receipt, or emolument. There is no evidence or suggestion that the money was sent to Mr Wing for any such reason as that he was in ill-health and required change of climate, or that he was tired and needed a holiday, or that he was poor (as in Turton v Cooper [(1)]), or had a large family, or that he was well-mannered, or good-looking, or kind to animals; or that he was a paragon of manliness or virtue. The evidence is quite clear. The letter which he received with the cheque requests him to accept it for his "very fine riding of Ballyheron at the Irish Derby.''*

In *Brumby v Milner* (1976) 51 TC 583, the issue was whether a distribution to employees from a profit-sharing trust established by their employer constituted an emolument arising from employment. In the House of Lords, Lord Kilbrandon reflected on the meaning of the concept of the payment arising for something other than the employment. At page 31, he stated;

> *'It is conceded that the income payments made from the trust fund to employees arose from their several employments and were properly taxable in their hands. It was therefore necessary for the Appellant to show that, by contrast, the payment out of capital, to use Lord Reid's words, "arose from something else". It was submitted that the payment arose not from the Appellant's employment but from the company's reluctant decision to wind up the profit-sharing scheme. I cannot agree with that. Certainly the money forming the payment became available in consequence of certain events and decisions connected with the structure of the company. But the sole reason for making the payment to the Appellant was that he was an employee, and the payment arose from his employment. It arose from nothing else, as it would have done if, for example, it had*

> *been made to an employee for some compassionate reason. In such a case, as Lord Reid pointed out in Laidler v Perry [1] (supra), at pages 31-2, "the gift is not made merely because the donee is an employee". There would be another reason personal to the recipient, namely his distress. There is no such other reason here.'*

In seeking to distinguish between a payment received *qua* employee and a payment received for some other reason, a fair comparison may be drawn between the language used by Lord Kilbrandon in *Brumby v Milner* and the language used by Kennedy CJ. in *Wing v O'Connell* above.

Returning to *Wing v O'Connell*, at page 107 of the report Fitzgibbon J., addressing the question of whether the £400 was a profit or earning of Mr. Wing's vocation, stated;

> *'The third main contention of the respondent is that the £400 was not a profit or earning of his employment or vocation. Prima facie, the capacity in which he received it is a question of fact, and the Commissioners have found that it was "an, emolument which arose or accrued to the appellant" (as he then was) "by reason of his vocation as jockey," and in my opinion the letter of Colonel Charteris enclosing the cheque furnished ample evidence to support that finding: "Please accept the enclosed present, with my very best thanks, for your very fine riding of Ballyheron in the Irish Derby. It was a very fine performance, and did you the greatest credit." The profession or vocation of the respondent was to ride horses in races, and he received the present "for his very fine riding" of a race-horse in an important race. The "fine performance'' was a feat of jockeyship, and it was as a jockey that it did him the greatest credit. I confess that I can find no evidence that he received this gift upon any consideration other than that of his professional services. It is not found, or even suggested, in the case that Colonel Charteris and Wing were upon terms which would influence the former to make a gift upon any other ground than that of a desire to reward exceptional merit as a jockey, or that there was any previous acquaintance between them.'*

In terms of this appeal, no evidence was led on behalf of the Appellant that the payment was made on compassionate or altruistic grounds or on grounds of ill-health or indigence or any grounds in the '*personal equation'* category set out above albeit, the examples cited above do not comprise an exhaustive list. Rather, it was contended that the payment was made on grounds of gratitude, friendship and admiration and that the payments formed part of either

the '*personal equation'* or Lord Reid's '*something else'* category and were not subject to income tax as a result.

In the UK Court of Appeal case of *Kuehne + Nagel Drinks Logistics v Revenue and Customs Commissioners* [2012] EWCA Civ 34, the Court took the view that a payment may arise from employment notwithstanding the fact that it is in part motivated by a feeling of generosity toward the recipient. Patten L.J. considered the issue of competing causes. He stated, at paragraphs 56-59:

> *'[56] I do not accept that this is a correct statement of the law but it does not, I think, arise on a proper reading of the judgment in this case. Mr Sykes criticised the judge for treating the loss of pension rights and the threat of industrial action as equal causes. I am not satisfied that on a fair reading of his judgment this is what the judge did. The highest that Judge Hellier put it was that a payment can be from employment even though there are other reasons for it: see para [103] of his judgment. This is obviously right. In all the cases I have referred to there are competing causes. Obvious examples are Laidler v Perry (Inspector of Taxes) (1965) 42 TC 351, [1966] AC 16 (staff Christmas bonuses) and Cooper (Surveyor of Taxes) v Blakiston (1908) 5 TC 347, [1909] AC 104 (an incumbent's Easter offerings). In each case the payments were in part motivated by feeling of generosity towards the recipient. Employment does not have to be the sole cause but it does have to be sufficiently substantial as to characterise the payment as one from employment.*
>
> *[57] The judge seems to me to have carried out this exercise. After stating the principle in para [103], he then identifies a substantial cause as the need to avoid strike action. On that basis, he decides in para [104] that the payment was taxable because it was paid for that purpose. The fact that it was also compensation for loss of pension rights does not affect that conclusion.*
>
> *[58] On a proper reading of his judgment this is, I think, a conventional approach to causation and clearly a correct one. The loss of pension rights was historically the source of the dispute but things moved on and the possibility of industrial action became the reason for the payment. Mr Sykes is therefore wrong to say that there was no weighing up, as he puts it, and on this basis I would dismiss the appeal.*
>
> *[59] But even if the correct view of the judge's findings of fact is that the loss of pension rights and the threat were equal rather than successive causes of the payments then the same conclusion must, I think, follow. It is impossible in those circumstances to say that the payments were not from the employment even though they were compensatory in*

> *nature. If the employment is a substantial and equal cause of the payment, it becomes open to the judge to say that the statutory test is satisfied. The payment is then from the employment even if it is also substantially attributable to a non-employment cause.'*

Similarly, in *Cooper v Blakiston* (1909) AC 104, it was held that the Easter offerings paid by a church to its vicar accrued to him by reason of his office. In *Cooper v Blakiston,* Lord Ashbourne observed:

> *'It was suggested that the offerings were made as personal gifts to the vicar as a mark of esteem and respect. Such reasons no doubt played their part in obtaining and increasing the amount of the offerings, but I cannot doubt that they were given to the vicar as vicar, and that they formed part of the profits occurring by reason of his office.'*

Turning to the letters of 14 June 2007 and 29 June 2007 received by the Appellant, in which the payors expressed their *'deep appreciation of your efforts and commitments through the period of our investment in the AB Group, culminating in the recent, very successful IPO'.*

The letters continue; *'Everyone at* [AB Feeder GP Limited/ XY Partners] *is conscious of the sacrifices that you made in this period of your life to deliver the exceptional return that we have achieved to date. In recognition of this and as a concrete expression of our gratitude, we have decided to make a gift to you of …..'*

In *Wing v O'Connell*, Kennedy C.J. questioned how one separates the individual from the professional when he stated;

> *'The vocation of a professional jockey is to engage himself for hire to ride horses in races with the professed object of winning or trying to win those races. He is paid by fees according to a scale framed by a governing authority, the Turf Club. The scale varies according to the results, success in winning the amount of the stakes. All jockeys cannot win all races but winning or trying to win is the professional objective of every racing engagement, so that there is, in my opinion, no foundation in fact for the attempt to separate the success as something purely personal from the riding, which is admittedly professional. Mr Leonard's metaphysics transcend the facts with which we have to deal.'*

A similar dilemma arises in this appeal in terms of whether it is possible to separate Mr. C.'s individual excellence from his role as CEO in circumstances where his individual excellence was demonstrated through his role as CEO.

In *Laidler v Perry* [1966] AC 16, Lord Reid stated;

> *'There is a wealth of authority on this matter and various glosses on or paraphrases of the words in the Act appear in judicial opinions, including speeches in this House. No doubt they were helpful in the circumstances of the cases in which they were used but in the end we must always return to the words in the statute and answer the question – did this profit arise from the employment? The answer will be "no" if it arose from something else.'*

Turning to the words of the statute, section 112 provides that income tax under Schedule E shall be charged ' .. *on every person having or exercising an office or employment of profit mentioned in that Schedule, or to whom any annuity, pension or stipend chargeable under that Schedule is payable, in respect of all salaries, fees, wages, perquisites or profits whatever therefrom, and shall be computed on the amount of all such salaries, fees, wages, perquisites or profits whatever therefrom for the year of assessment.*

The June 2007 letters denote that the payments made to the Appellant of *€1,075,150* and *€1,224,850*, were for the exceptional work carried out by the Appellant which led to the very successful IPO in 2007.

The gratitude expressed by the payors was gratitude for the Appellant's work '*through the period of our investment in the AB Group culminating in the recent, very successful IPO'* which delivered for the shareholders '*the exceptional return that we have achieved to date'*. The Appellant in his submission sought to separate the gratitude from the work but the reality is, and the words of the letters make clear, that the gratitude was expressed in relation to the Appellant's work and was directly related to it.

The payments made to the Appellant were not made on grounds of compassion, altruism, ill-health, indigence or other similar reasons. In addition, the fact that this was not a payment to the Appellant alone, but a payment that was made to all four members of the senior executive team, is significant. It removes any argument that the payment made to the Appellant was exceptional or in any way purely personal to him or that the payment was made to him for

personal reasons. As a result, I am satisfied that the payments received did not form part of the personal equation. Nor were the payments made '*from something else*' per the dicta of Lord Reid in *Laidler v Perry*.

In *Weight v Salmon* (1935) 19 TC 134 the taxpayer was a managing director of a limited company and was entitled under a service agreement to a fixed salary. In addition, the directors of the company by resolution each year gave the Respondent the privilege of applying for certain unissued shares in the company at their par value, which was considerably less than their current market value. It was held that the privilege granted to the taxpayer represented money's worth and was assessable to Income Tax as a profit of his office as managing director. Finlay J. stated that *'It was a payment made to Mr. Harry Salmon because he was a Managing Director and because in that capacity he had managed the business so successfully and so skilful.'*

The payments received by Mr. C. were made by the private equity firms, the shareholders in ABG, as a payment for the exceptional services rendered by him. It is not possible to separate Mr. C.'s individual excellence, from his role as CEO in circumstances where the manner of demonstrating his excellence was by being CEO, by acting as CEO and by delivering exceptional results as CEO.

3) Contractual obligation and voluntariness

The fact that a payment is made voluntarily does not mean that the payment is not taxable as an emolument under Schedule E. The absence of a legal obligation on the payor to make the payment does not prevent it being taxable as earnings. The mere fact that a payment involves generosity on the part of the payor does not prevent the payment being assessable to tax as an emolument.

On page 103 of *Wing v O'Connell*, Kennedy C.J. stated;

> '*I am, therefore, of opinion that the sum of £400 in question in this case was not paid to or received by Mr Wing as a pure gift or present, but that it was given to him for, that is to say, in consideration of, professional work done and vocational services rendered in successfully steering the horse, Ballyheron, to victory, in other words, for successfully accomplishing the object of his professional engagement, and that it was in the nature of a bonus or voluntary addition to the prescribed fee under the regulation scale.'*

I am of opinion that it makes no difference in arriving at this view that the payment was on the part of Colonel Charteris voluntary in the sense that he was not bound by any legal contractual obligation to give it. My view is also arrived at without regard to any practice which may exist as to making such gifts and without regard to any expectation on the part of the jockey that his successes will be acknowledged in this way.'

In *Wing v O'Connell*, at page 106, Fitzgibbon J. addresses the issue of taxation in relation to a voluntary payment. He stated as follows;

'Upon the second question it appears to me to be settled law—upon principles with which I can find no fault—that the voluntary character of the payment, viewed from the standpoint of the donor, does not necessarily exempt it from liability to assessment in the hands of the recipient. .... The same point came before the English Court of Appeal in 1902 in Herbert v M'Quade, where it was held that a beneficed clergyman of the Church of England was liable to pay income tax upon a grant in augmentation of the income of his benefice received on more than one occasion from a society called the Queen Victoria Clergy Sustentation Fund. In that case Collins MR, after citing the judgment of Lord Curriehill in Inland Revenue v Strong, stated:

'Now that judgment, whether or not the particular facts justified it, is certainly an affirmation of a principle of law that a payment may be liable to income tax although it is voluntary on the part of the persons who made it, and that the test is whether, from the standpoint of the person who receives it, it accrues to him in virtue of his office; if it does, it does not matter whether it was voluntary or whether it was compulsory on the part of the persons who paid it. That seems to me to be the test; and if we once get to this—that the money has come to, or accrued to, a person by virtue of his office—it seems to me that the liability to income tax is not negatived merely by reason of the fact that there was no legal obligation on the part of the persons who contributed the money to pay it.''

The cases of *Herbert v McQuade* (1902) 4 TC 489 and *Cooper v Blakiston* (1909) AC 104 both involved voluntary payments. In the former case, Stirling LJ stated: ' *.... a profit accrues by reason of an office when it comes to the holder of the office as such – in that capacity – and without the fulfilment of any further or other condition on his part.*' In *Cooper v Blakiston*, the Lord Chancellor stated; *'In my opinion, where a sum of money is given to an incumbent substantially in respect of his services as incumbent, it accrues to him by reason of his office.'*

Fitzgibbon J. in *Wing v O'Connell* at page 108, quoted the following from *Cooper v Blakiston*

> *'First, it is immaterial that these offerings were made voluntarily. There are many professions and callings in which income is derived from payments voluntarily made.*
>
> *The question is not what was the motive of the payment, but what was the character in which the recipient received it? '*

The Appellant in the within appeal argued that there was no contractual obligation on the shareholders to make the payment to him and that this supported his submission that the payment was a gift however, based on the Irish Supreme Court authority of *Wing v O'Connell*, the absence of a contractual obligation to make the payment does not determine the nature of the payment and a payment may be entirely voluntary and be taxable as an emolument notwithstanding.

4) Expectation

On page 103 of Wing v O'Connell, Kennedy C.J. stated;

> '*I am, therefore, of opinion that the sum of £400 in question in this case was not paid to or received by Mr Wing as a pure gift or present, but that it was given to him for, that is to say, in consideration of, professional work done and vocational services rendered in successfully steering the horse, Ballyheron, to victory, in other words, for successfully accomplishing the object of his professional engagement, and that it was in the nature of a bonus or voluntary addition to the prescribed fee under the regulation scale.'*
>
> *I am of opinion that it makes no difference in arriving at this view that the payment was on the part of Colonel Charteris voluntary in the sense that he was not bound by any legal contractual obligation to give it. My view is also arrived at without regard to any practice which may exist as to making such gifts and without regard to any expectation on the part of the jockey that his successes will be acknowledged in this way.'*

[emphasis added]

Mr. C. gave evidence that the payment was unexpected however, Irish law does not treat expectation on the part of the recipient as relevant to the question of whether the payment is

taxable in the hands of the recipient as arising from employment. The UK authorities which differ from Irish law in this respect, must give way to the binding Irish Supreme Court authority of *Wing v O'Connell*.

5) Exceptionality

In *Wing v O'Connell*, Fitzgibbon J. on page 111 of the report stated;

> *'Two minor points remain to be noticed. It has been suggested that a voluntary gift of the description in question cannot be liable to taxation unless it is recurrent, or unless it is of a kind which the recipient has a reasonable expectation that he may receive. I admit that in some of the judgments which reversed the decisions of the Commissioners or of a Court of first instance there are expressions indicating that reliance was placed either upon the recurrence of the grant, or, as in the case of the cricketer, upon the probability of a benefit match; but I cannot find that they are founded upon any question of principle. If a sum of money is a profit of a trade, it must be so each time it accrues; and I cannot see, upon principle, why a second windfall should be taxable if the first is not, or why, if the second, third, and fourth be taxable, the first is not equally so. Nor can I understand why, if a man receives extraordinary remuneration for his professional services, it should be any the less an earning of his profession because he did not expect such liberal treatment.'*

The Appellant's evidence was that he did not expect the payment and that it was extraordinary. The Respondent challenged this evidence on the basis that a proportionally equal payment was made to all four members of the senior executive team including the Appellant and that the payment was therefore not personal to the Appellant, was not a one-off and was not extraordinary. I accept the submission of the Respondent in this regard.

In conclusion on this point and as a matter of Irish law, the extraordinary or one-off nature of the payment is not a factor of significance having regard to the dicta of Fitzgibbon J. in *Wing v O'Connell*.

In addition to the above, the case of *Bray v Best* 61 TC 705 is authority for the proposition that the payment does not need to be a recurrent payment to be subject to income tax as an emolument.

Contemporaneous Documentation

A. The importance of contemporaneous records

In *McBride v Blackburn [2003] STC (SCD) 139*, a UK Special Commissioners' decision, the Commissioners' emphasised the importance of contemporaneous records. The facts of the case are set out in the headnote which provides as follows;

> *'M was a Lloyd's name and a member of two groups of Lloyd's syndicates. From 1992 names began to form action groups, or associations, through which to pursue their claims against Lloyd's agents, insurers, actuaries and Lloyd's itself (the Lloyd's defendants) for negligence and breach of fiduciary duty. M was chairman of one association and deputy chairman of another. He was not paid for his work. In 1996 settlement between the names and the Lloyd's defendants was close. As part of their offer Lloyd's offered to pay general damages, legal costs and expenses refunds. There were discussions within the associations about committee remuneration and ex gratia payments to the associations' officers. Payments were considered on the bases of the workload of the committee members, the responsibilities they had each undertaken, and the secretarial work they had assumed on behalf of the associations. After authorisation at general meetings the two associations made to M, after he had resigned from office, payments amounting to £280,000 expressed to be ex gratia. The Revenue assessed M to tax on the basis that the payments were in the nature of remuneration and taxable under Sch E as emoluments from an office under s 19 of the Income and Corporation Taxes Act 1988. M appealed, contending that the payments were not liable to tax as they were gifts of an exceptional nature paid to him personally and not for his work or services.'*

Paragraph 57 of the decision provides;

> *'In assessing the weight to give to the oral evidence of the appellant and Mr. Smallbone we test it against the contemporaneous documents.'*

Paragraph 62 continues:

> *'This answer to the question 'what were the payments made for?' is consistent both with the payments being emoluments of the respective offices of the officers (including the appellant) and the committee members …. We find, however, that the weight of the*

indicia in the contemporaneous documents overwhelmingly points towards each of the payments being emoluments within s 19, ….. '

Thus, it's clear that *McBride v Blackburn*, a decision of persuasive authority, is an important decision in terms of identifying the significance of contemporaneous records and the weight that may be attributed to contemporaneous records in the adjudication process.

The contemporaneous documents in the within appeal which I shall now examine are;

- the June 2007 letters from the shareholders
- the 2007 Annual Report of AB plc.
- minutes of AB Feeder G.P. Limited (Jersey entity) on 28 June 2007 and
- the XYCP Global Aggregator Limited Partnership Agreement

B. <u>The June 2007 letters</u>

The letters written by the payors, dated 14 June 2007, and 29 June 2007 respectively, provide as follows;

The letter dated 29 June 2007 from AB Feeder GP Ltd. provided;

'Dear Mr. C.

AB Feeder L.P. (the "Limited Partnership")
Investment in AB Group

We are writing to express our deep appreciation of your efforts and commitments through the period of our investment in the AB Group, culminating in the recent, very successful IPO. Everyone at AB Feeder GP Limited is conscious of the sacrifices that you made in this period of your life to deliver the exceptional return that we have achieved to date.
In recognition of this and as a concrete expression of our gratitude, we have decided to make a gift to you of €1,224,850. We will, of course, expect that you will comply with all of your obligations as to disclosure and taxation in respect of our gift.
We intend on making payment to you shortly after we achieve liquidity in respect of a significant part of our shareholding in AB Group.

Yours sincerely

For an on behalf of
AB Feeder G.P. Limited
As General Partners on behalf of
AB Feeder L.P.'

The letter dated 14 June 2007 from XY Partners provided:

'Re: Our Investment in ABG

Dear Mr. C.,

I am writing to express our deep appreciation of your efforts and commitment throughout the period of our investment in AB Group, culminating in the recent, very successful IPO. Everyone at XY Partners is conscious of the sacrifices that you made in this period of your life to deliver the exceptional return that we have achieved to date.

In recognition of this and as a concrete expression of our gratitude, we have decided to make a gift to you of €1,075,150. We will, of course, expect that you will comply with all of your obligations as to disclosure and taxation in respect of our gift.

We intend on making payment to you shortly after we achieve liquidity in respect of a significant part of our shareholding in AB Group.

Yours sincerely

Mr. D'

It is clear from the June 2007 letters that with the exception of the specification of the monetary amounts and the references to the payors, the letters are written in exactly the same terms.

In his letter, Mr. D. refers to the extensive work undertaken by the Appellant '*throughout the period of our investment*' i.e. in the period from 2002 to the successful IPO in 2007. In the

letter Mr. D. wrote; '*Everyone at XY Partners is conscious of the sacrifices that you made in this period of your life to deliver the exceptional return that we have achieved to date.*

During re-examination of Mr. D. by QC for the Appellant, Mr. D. was asked what he meant by the reference to '*sacrifices'* in the letter and Mr. D. responded;

> *'.. what I am referring to there is what I mentioned earlier which is in my 36 years in this business I have never seen a chief executive officer work as hard as Mr. C. with as much commitment… My partners at XY were aware of that. You know Mr. C. works…, worked non-stop, weekends, you name it, he was working. It was beyond anything I had ever seen. It was beyond anything that Mr. E. or Mr. K. had ever seen. It was extraordinary, it was extraordinary. It was incredible leadership for the organisation and it's really that extraordinary leadership that we felt grateful for. That's what I am getting at in that letter.'*

Thus, the payors were expressing their appreciation for the enormous amount of work undertaken by Mr. C. while they were shareholders over the period 2002-2007. The letter is thanking the Appellant for the substantial return made in relation to their investments, as a result of the work carried out by Mr. C. over this period. Mr. D., in paragraph 23 of this witness statement stated; *'It was easier operationally to pay the amount out of the proceeds of the sale of the ABG shares. The amount of 5.8 million needs to be viewed in the context of overall result where circa US$450 million was invested and what came out was circa US$800 million.'*

Of course, the Appellant placed reliance on the letters in support of his submission. He relied on the description of the payments as a '*gift*'. However, it is important to note that the label used by the payor/recipient to describe a payment is not determinative of the nature or character of that payment for tax purposes as can be seen from *Wing v O'Connell* where the payment was described as a '*present'* but was held to be taxable as an emolument and subject to income tax.

On the issue of the intention or motivation of a payor, the position is that the intention or motivation of the payor is not determinative of the nature or character of that payment for tax purposes and this principle is supported by the dicta of Fitzgibbon J. in *Wing v O'Connell* where at page 108, he quoted the following from *Cooper v Blakiston; 'The question is not what was the motive of the payment, but what was the character in which the recipient received it?*

Thus, even if the payors in this appeal intended to make a gift of the sum of €2.3m to the Appellant (a proposition the Respondent disputed on the basis of descriptions of the payment in certain documents as an '*IPO Bonus*'), their intentions do not determine the character of the payment for tax purposes, rather, the transaction itself must be objectively considered. This is consistent with the dicta of Fitzgibbon J. in *Wing v O'Connell* where at page 108, he quoted the following from *Cooper v Blakiston*

> *'The question is not what was the motive of the payment, but what was the character in which the recipient received it? '*

Fitzgibbon J. continued on page 109, as follows

> *'I do not hold that the motives of the donor are and must always be immaterial, but I do hold that where the profit accrues to the recipient in consequence of services rendered by him in his professional capacity and as a reward for those services, the charitable or other motives actuating the donor do not exempt the donation from liability to tax. On the other hand, if the donation is actuated by a desire to remunerate a professional man for services rendered in his professional capacity, it will be liable to tax, though the recipient may have no legal claim upon it. In other words, if the gift is either given or taken as a reward for professional services, it is a profit or earning of the profession.'*

In addition to the Appellant's submissions on the description of the payment as a gift and the intentions of the payors to make a gift to the Appellant, the Appellant submitted that the payment was voluntary in nature and that this indicated that the payment was, a gift. In his witness statement the Appellant stated; *'Given our work ethic there was solidarity between Mr. D. and me. I had no expectations that a gift would be made. If the gift had never been made I would have been perfectly happy, not expecting the gift in the first instance.* As against that, the Respondent contended that the payment was a bonus in recognition of work undertaken by the Appellant during the years 2002-2007, culminating in the successful IPO in March 2007.

As evidenced by the Irish Supreme Court authority of *Wing v O'Connell*, a payment may be voluntary and be taxable as an emolument notwithstanding. Thus, I attach minimal weight to this consideration.

In *Allum v Marsh* [2005] STC (SCD) 191, a company made voluntary payments of £30,000 each to two former directors '*following the resignation due to retirement … in appreciation of*

their services to the company over many years'. The question for consideration was whether the payments constituted emoluments from an office or employment in accordance with section 19 of the UK Corporation Taxes Act 1988. Dr Brice, Special Commissioner, addressed this question at paragraph 62 of the decision as follows;

> *'62. Mr Wilson for the appellants argued that the voluntary payments were not emoluments of the offices of directors held by Mr and Mrs Allum because on the date that the payments were voted by the company Mr and Mrs Allum had resigned as directors and had therefore ceased to hold those offices. The payments, therefore, were not 'from' the employment.'*

At paragraph 65 the Commissioner continued;

> *'65. In applying these principles to the facts of the present appeal I first consider the minute of the meeting on 24 March 2001 which made it clear that the payments were made 'in appreciation of the services [of the appellants] to the company over many years'. It seems to me that the minute supports the conclusion that the payments were made in respect of the discharge of the duties of the offices of directors held by the appellants. They were voluntary payments made in recognition of services rendered. The payments accrued to the appellants by virtue of their offices as directors. They were not testimonials, nor were they peculiarly due to the personal qualities of the appellants, nor were they a mere present, nor were they made irrespective of and without regard to the services rendered. The payments were made by the company of which the appellants had, for very many years, been directors. They were made in return for the appellants acting as and being the directors. They were, therefore emoluments and taxable under s 19.'*

A comparison may be drawn between the language used by the payors in this appeal, in the June 2007 letters, where they stated that they were:

> *'writing to express our deep appreciation of your efforts and commitment throughout the period of our investment…'*

and the language used in *Allum v Marsh*, namely;

> *'… in appreciation of their services to the company over many years'.*

In addition (as set out above) Mr. D., referring to the payment received by the Appellant, on the second day of hearing stated; *'...it was intended to demonstrate respect and appreciation for the hard work and dedication shown'*.

In direct examination, Mr. D. was asked; *'Was the amount of the gift dependent on your profit on the disposal of your ultimate exit?*' to which Mr. D. replied; *'No, it had nothing to do with our profit on the disposal, it had nothing to do with that at all. It was purely an expression of gratitude, of admiration, or appreciation for incredibly hard work and dedication over the life of our investment and culminating in the IPO, to getting it done.'*

While evidence in this appeal indicated that non-contractual payments by private equity houses to their executives, are a relative rarity, the Respondent pointed out that all four senior executives in ABG (including the Appellant) were rewarded in proportionally the same manner as the Appellant. The Respondent emphasised that there was no additional payment made to the Appellant, in recognition of his exceptionality, over and above the three other members of the executive team and I accept this submission on behalf of the Respondent.

Thus, in conclusion under this sub-head;

- the description of the payment as a 'gift' in the June 2007 letters does not characterise or determine the nature of the payment for tax purposes and I attach minimal weight to this description in accordance with the Irish Supreme Court authority of *Wing v O'Connell*.
- In accordance with *Wing v O'Connell,* the intention or motivation of the payor is not determinative of the nature or character of that payment for tax purposes, rather, the transaction, its facts and circumstances, must be objectively considered.
- The Appellant submitted that the payment did not arise from the Appellant's employment, but it is difficult to reconcile this position with the sentiments expressed in the June 2007 letters ('*I am writing to express our deep appreciation of your efforts and commitment throughout the period of our investment in AB Group, culminating in the recent, very successful IPO. Everyone at XY Partners is conscious of the sacrifices that you made in this period of your life to deliver the exceptional return that we have achieved to date. In recognition of this…..').* It is also difficult to reconcile the Appellant's position with the evidence of Mr. D. including, his statement that *'...it was*

intended to demonstrate respect and appreciation for the hard work and dedication shown'.

- Taking into account the June 2007 letters and their content and the evidence of Mr. D., I am satisfied that the gratitude expressed in the June 2007 letters related to the services rendered by the Appellant over the period of his employment from 2002 to 2007 and that the payments made to the Appellant, arose in that context.
- The matter of the fact that this payment was made in equal proportions to three other members of the senior executive team is a relevant consideration as it mitigates the position put by the Appellant that the payment of €2.3m received by him was exceptional in nature.

C. The 2007 Annual Report of AB plc

The remuneration report contained at page 49 of the AB Group plc Annual Report for the year ended 31 December 2007 provides (paraphrased);

> *In June 2007, a cash amount of approximately €5.8 million was awarded to the executive Directors (€5.3million) and the Company Secretary by the major shareholders XY Capital Partners and AB Feeder GP Limited and is payable directly by those shareholders. The award was made in connection with the successful flotation of the Company.*
>
> [emphasis added]

This statement was repeated on page 149 of that Report. While the annual report was produced the year following the June 2007 letters, and is not therefore strictly contemporaneous, it is near contemporaneous. Further, it is an independent document generated to satisfy, *inter alia*, company law reporting requirements.

The statement above is consistent with the June 2007 letters insofar as it suggests that these payments were made in recognition of work undertaken by the Appellant and his fellow executives in bringing the company to a point where it was in a position to progress a successful IPO.

During cross-examination of the Appellant on day two of the hearing, the following exchange occurred in relation to the above quoted statement in the remuneration report;

'A. .. my starting point was and is I was surprised, in the circumstances, that we need to report this. However, my CFO and our finance people in general and our auditors and technical advisors on the audit reliably informed me and indeed the Audit Committee and the Board that this was required and that this was probably the correct way to report it. Based on that advice , I –

Q. So based on that advice, this was the correct way to report it?

A. As I understand it. And therefore, that was signed.

Q. Okay. Not as a gift?

A. I was advised this was the way we had to report it.

Q. I appreciate that. But the advice was not to describe it as a gift?

A. No, no, the advice was to report it exactly as it is.

Q. Yeah, where there's no indication that it's given as a gift, instead it's an award made in connection with the successful flotation of the company; isn't that right?

A. Absolutely.

Q. Yeah.

A. The words are there.

Q. And I'd have to suggest to you that language is redolent of the language that we saw yesterday in the internal documents of AB Feeder where it was described as an IPO bonus.

A. That's what the words said, yes.'

Thus, in conclusion under this head; the Appellant submitted that the statement in the annual report that *The award was made in connection with the successful flotation of the Company* could be explained on the basis that the statement was required on foot of the auditors' and CFO's advice but that greater importance could be attributed to *inter alia*; the description of

the payments as a '*gift*' in the 2007 letters, the motivation of the payors and the fact that the payment was, in 2007, voluntary and unexpected.

As set out above, in accordance with *Wing v O'Connell*, it matters not that the payment made was spontaneous, unexpected or voluntary. The Appellant sought to rely on the UK First Tier Tribunal case of *Colin Collins* v *Revenue Customs Commissioners* [2012] UKFTT 411 where the '*gratuitous and unexpected*' nature of the payment was taken into consideration by the Tribunal however, the *Collins* case can be distinguished from the within appeal on a number of grounds including; that the Appellant in that case had ceased to work four years prior to receiving the payment, that the donor in that case had sold the company 18 months prior to making the payment and that the sum received by the Appellant in that case was described at page 20 of the report as being '*wholly disproportionate to the amount of the Appellant's past salary*' whereas the €2.3m paid to the Appellant was not disproportional to his salary, rather, it was twice his salary.

As regards the label given to the payment by the parties, labels are not determinative of the character of the payment. In determining the true nature of a payment, it is necessary to look at the substance of the payment. In this regard the use of the words '*award*' and '*awarded*' in the Annual Report are significant and are at odds with the reference to 'gift' in each of the letters from XYCPGALP and ABFGP in June 2007. In this regard, it is clear that the description or label given to a payment by the payor is irrelevant. For example, in *Radcliffe v Holt* (1927) 11 TC 621, a payment described as a '*gift*' was held to be assessable to income tax on the basis that the payment was remuneration arising from the Respondent's office. In addition, the payment in *Wing v O'Connell* which was described as a '*present*' was found to be assessable to tax as an emolument.

D. <u>The minutes of AB Feeder G.P. Limited (Jersey entity) dated 28 June 2007</u>

Another relevant document is the minutes of the Jersey entity, AB Feeder G.P. Limited, dated 28 June 2007, a contemporaneous document. This document contains the decision of the Jersey entity to issue a letter in similar terms to the letter sent by Mr. D., on 14 June 2007. AB Feeder G.P. Limited, sent a letter in these terms on 29 June 2007.

The minutes provide;

> *'3. Business of the Meeting*

3.1 The Chairman reported that the meeting had been convened to consider and, if thought fit, approve IPO bonuses (the 'Bonuses'), as detailed within the meeting documentation circulated, to members of the AB Management team (the 'Recipients') in appreciation for their efforts and commitments throughout the period of our Investment in The Company, cumulating (sic) in the recent, successful IPO.'

Leaving aside the reference to '*gift*', the above statement is consistent with the sentiments expressed in the June 2007 letters. The descriptions suggest that the sum was paid in relation to work done in bringing the company to a state where the company could be successfully re-floated.

E. <u>The Limited Partnership Agreement of XYCP Global Aggregator L.P.</u>

The opening clause of the XYCP Global Aggregator limited partnership agreement provides that XYCP Global Investments limited, a Cayman Islands exempted company, is the general partner in XYCP Global Aggregator L.P.

Paragraph 3.4 of the agreement provides that the general partner '*shall be entitled to pay on behalf of the Partnership all Partnership Expenses*'.

The agreement provides at paragraph 3.4 that *'<u>Partnership expenses means all expenses incurred by the Partnership in connection with the conduct of its business,</u> including any costs and expenses relating to the Partnership's existence under the Partnership Act, any taxes, fees or other charges levied against the Partnership or on the Partnership's income or assets or in connection with the Partnership's investment by any national government, any state or other political subdivision thereof, or any entity exercising executive, legislative, judicial, regulatory or administrative functions of government and any amounts necessary to satisfy the Partnership's indemnification obligations that may arise from time to time pursuant to section 4.2 hereof.'*

[emphasis added]

In short, the agreement provides that partnership expenses are *'... expenses incurred by the Partnership in connection with the conduct of its business..'.* It follows that if the payment to the Appellant were by reason of friendship or admiration, as submitted on behalf of the Appellant, the payment would not comprise a payment in respect of the conduct of the business of the partnership.

On the other hand, if the payment were in respect of work done by the Appellant, as submitted on behalf of the Respondent, then the payment would constitute an expense incurred by the partnership in connection with the conduct of its business.

While Mr. D. may have been friends with Mr. C. the limited partnership could not have been a friend. The general partner was a Cayman Islands company and the general partner of a limited partnership cannot be a friend. A company cannot be friends with a human person. It is legally impossible for a friendship to exist between a limited company in the Cayman Islands and the Appellant. It is legally impossible for a general partner or a limited partnership to be friends with anyone.

Even if, legally speaking, the limited partnerships, or the limited companies forming the general partners of the limited partnerships could be said to have a relationship of friendship with the Appellant, the fact is that there was no friendship between them and no relationship of any kind.

This is acknowledged by Mr. D. on day two of the hearing, when the following exchange occurred under cross-examination by Senior Counsel for the Respondent;

> *'Q: And the underlying investors in the AB Feeder Ltd. partnership in Jersey didn't have any relationship with Mr. C. –*
>
> *A: Right*
>
> *Q: - or any friendship with Mr. C.?*
>
> *A: Yeah, in the same way that our limited partners..*
>
> *Q: Didn't?*
>
> *A: Didn't '*

Thus, the people funding the payment to the Appellant had no relationship or friendship with the Appellant. The payment, the subject of this appeal, was not made by Mr. D. personally nor was it made by the Appellant's employer, ABG. It was made by the underlying investors in ABG. While Mr. D. classified the payment as a '*gift*' it was not his money that the Appellant received.

Additional case law and analysis

(i) The importance of statutory language

In *Brumby v Milner* (1976) 51 TC 583, the issue was whether a distribution to employees from a profit-sharing trust established by their employer constituted an emolument arising from employment. In that case the judgment of Walton J. in the Chancery Division was upheld by both the Court of Appeal and the House of Lords. At page 17 of the judgment, Walton J. refers to the *causa causans* language in the judgment of Jenkins L.J. in *Hochstrasser v Mayes* (1959) 38 TC 673, which, in the words of Jenkins L.J. was introduced as follows;

> *'I think it may well be said here that, while the employee's employment by I.C.I. was a causa sine qua non of his entering into the housing agreement and consequently, in the events which happened, receiving a payment from I.C.I., the causa causans was the distinct contractual relationship subsisting between I.C.I. and the employee under the housing agreement, coupled of course with the event of the house declining in value.'*

Walton J. stated;

> *'This test was repeated by Lord Simonds in the House of Lords, and the actual passage I have cited was also approved by Lord Cohen. But this is not the statutory language, and for less gifted mortals than these three I think it is perhaps less conducive to error to stick closely to the statutory language…..*

The House of Lords in *Brumby v Milner* firmly rejected the *causa causans* method of reasoning and accepted the approach taken by both Walton J. and the Court of Appeal.

In the recent UK Court of Appeal case of *Kuehne v Nagel Drinks Logistics* [2012] STC 840, the Court made some preliminary observations which indicated a move away from theoretical type analysis and a return toward identifying a link between the payments to employees and their employment, see paragraphs 31-33 of the judgment, under the heading '*discussion and conclusions*'.

In *Laidler v Perry* [1966] AC 16, Lord Reid stated;

> *'There is a wealth of authority on this matter and various glosses on or paraphrases of the words in the Act appear in judicial opinions, including speeches in this House. No doubt they were helpful in the circumstances of the cases in which they were used <u>but in the end we must always return to the words in the statute and answer the question – did this profit arise from the employment?</u> The answer will be "no" if it arose from something else.'*

[emphasis added]

This sentiment was echoed by Walton J. in *Brumby v Milner* (1976) 51 TC, who stated '*…I think it is perhaps less conducive to error to stick closely to the statutory language…'* and in the UK Court of Appeal case of *Kuehne* above where Mummery L.J. stated: '*The sovereign words are in the statute and not in the judicial exposition of it.'*

A convergence of approach in the more recent English authorities with the approach taken in 1926 by our Supreme Court in *Wing v O'Connell,* is apparent. One sees a retreat from the philosophical abstractions in *Hochstrasser v Mayes* and a return to the statutory language and the meaning of '*therefrom*' and the question of whether the payment arose from the employment.

Turning to the words of the statute, section 112 provides that income tax under Schedule E shall be charged ' .. *on every person having or exercising an office or employment of profit mentioned in that Schedule, or to whom any annuity, pension or stipend chargeable under that Schedule is payable, in respect of all salaries, fees, wages, perquisites or profits whatever <u>therefrom</u>, and shall be computed on the amount of all such salaries, fees, wages, perquisites or profits whatever therefrom for the year of assessment.*

[emphasis added]

The question which arises from the statutory language and in particular, from the use of the word '*therefrom*' is whether the payment received by the Appellant arose from his employment with ABG. QC for the Appellant submitted that *'… in exceptional cases, working as an employee generates recognition, gratitude or a sense of moral obligation, and where this leads to a receipt, that receipt is not one of remuneration but something else…. In those exceptional cases, that something else is not taxable because the operative cause, or reason behind the payment, is not the employment but the recognition, gratitude or sense of moral obligation.'*

This was echoed by Mr. D. who stated in evidence on day two of the hearing '*The background to this gift is the admiration which I felt in respect of Mr. C. and the rest of the team for their immense dedication and commitment. This was something extraordinary and very rare*'.

Mr. D., referring to the payment received by the Appellant, stated: *'…it was intended to demonstrate respect and appreciation for the hard work and dedication shown'*. He continued*; 'It was recognition of Mr. C.'s sacrifice, my admiration and our friendship*.'

In direct examination, Mr. D. was asked; *'Was the amount of the gift dependent on your profit on the disposal of your ultimate exit?*' to which Mr. D. responded; *'No, it had nothing to do with our profit on the disposal, it had nothing to do with that at all. It was purely an expression of gratitude, of admiration, of appreciation for incredibly hard work and dedication over the life of our investment and culminating in the IPO, to getting it done.'*

Submissions and evidence lead on behalf of the Appellant consistently describe the gratitude as being for the hard work, dedication and commitment of the Appellant in carrying out the work which culminated in the successful IPO, echoing the words of the payors contained in the June 2007 letters which also expressed '*deep appreciation'* and '*gratitude'.*

The Appellant in his submission in relation to section 112 TCA 1997, sought to separate the gratitude from the work done, on the basis that his exemplary work performance was an attribute personal to him and that as a result, the payment did not arise from the employment but arose from reasons personal to the Appellant, unrelated to his employment. QC for the Appellant contended that this gratitude could stand apart from the employment. On day four of the hearing, he stated; *'And my submission is the law is correctly stated in McBride v Blackburn and, simply put, something can be a gift even if it flows, even if the gratitude flows from the employment, provided it is genuinely more an expression of generosity than something which flows naturally from the employment.'*

Based on the authorities including in particular, the dicta of Kenned CJ in *Wing v O'Connell ('there is … no foundation in fact for the attempt to separate the success as something purely personal from the riding…')* I cannot accept the submission of the Appellant, that the gratitude expressed by the shareholders stands alone and falls outside the remit of section 112 TCA 1997 nor do I accept that the payment arose in relation to '*something else'* per the dicta of Lord Reid in *Laidler v Perry.*

The payments received by Mr. C. were made by the private equity firms (the shareholders in ABG) for the exceptional services rendered by Mr. C. which allowed the shareholders to recover well on their investments. I do not accept that it is possible to separate Mr. C.'s individual excellence from his role as CEO in circumstances where the manner of demonstrating his excellence was by being CEO, by acting as CEO and by delivering exceptional results as CEO.

The payments in this appeal were not motivated by compassion, altruism nor were they made on grounds of ill-health or indigence. I do not accept that the payments received by the Appellant form part of the personal equation.

It has been established, based on the evidence, that the gratitude expressed by the paying shareholders related to the work carried out by the Appellant. In accordance with the Irish authorities, there is no basis for separating the Appellant's individual excellence from the employment through which that excellence was demonstrated. In conclusion, there is no obstacle to characterising the payment as one that arises *from* employment and one that is assessable to income tax in accordance with Schedule E.

(ii) Payments 'from' employment and arising 'therefrom'.

In *Laidler v Perry* [1966] AC 16, Lord Reid stated; ' …. *but in the end we must always return to the words in the statute and answer the question – did this profit arise from the employment? The answer will be "no" if it arose from something else.'*

Laidler v Perry is authority for the proposition that taxable emoluments are not confined to emoluments from the employer but embrace all payments received from the employment.

In the House of Lords case of *Bray v Best* 61 TC 705, Lord Oliver of Aylmerton quoted Lord Radcliff in *Hochstrasser v Mayes* and stated;

> *'Lord Radcliffe in the same case pointed out that all the various expressions which had been used to test whether particular payments arose "from" an employment (such as payments "made to an employee as such" or "in his capacity as an employee" or "by way of remuneration for his services") were no more than glosses on the statutory language which might be illustrative but could not be treated as definitive. "For my part", he observed .. "I think that their meaning is adequately conveyed by saying that, while it is*

not sufficient to render a payment assessable that an employee would not have received it unless he had been an employee, it is assessable if it has been paid to him in return for acting as or being an employee'

In the recent UK Court of Appeal case of *Kuehne v Nagel Drinks Logistics* [2012] STC 840, the Court made some preliminary observations which indicated a move away from theoretical style analysis and toward identifying a link between the payments to employees and their employment, see paragraphs 31-33 of under the heading '*discussion and conclusions*'.

In addition, Lord Justice Patten, in his judgment in that case at paragraphs 51 and 52 stated:

'[51] The ways in which that necessary link has been described and analysed in the earlier cases does, I think, have to be respected even though the ultimate question is whether the 'from' question can be answered in the affirmative. Neill LJ in Hamblett v Godfrey (Inspector of Taxes) [1987] STC 60 at 70, [1987] 1 WLR 357 at 370 describes those explanations as valuable and authoritative. And what the cases, I think, show is that the question of taxability involves one being able to characterise the payment as one 'from employment' if it derives 'from being or becoming an employee' and is not attributable to something else such as a mark of esteem or a desire to relieve distress. I take this formulation from Lord Templeman in Shilton v Wilmshurst (Inspector of Taxes) [1991] STC 88 at 91, [1991] 1 AC 684 at 689 because this is how the words 'from employment' were construed and that decision is, I believe, binding on us in that respect. The same test was adopted by Lord Reid in Laidler v Perry (Inspector of Taxes) (1965) 42 TC 351 at 363, [1966] AC 16 at 30 and by Lord Kilbrandon in Brumby (Inspector of Taxes) v Milner [1976] STC 534 at 538, [1976] 1 WLR 1096 at 1101.

[52] It must follow from this that, in order to satisfy the s 9 test, one must be able to say that the payment is from employment rather than from a non-employment source. This has certainly been the approach of the courts in most of the decided cases …

…..

[55] The criticism of the judge is that he did not decide what was the dominant cause of the payment or, in the language of s 9, whether it was from the employment and HMRC has responded to this with their arguments to the effect that a contributing cause which is more than marginal but which is an employment-based cause can bring the payment into charge even if there are other substantial non-employment causes.

> *[56] I do not accept that this is a correct statement of the law but it does not, I think, arise on a proper reading of the judgment in this case. Mr Sykes criticised the judge for treating the loss of pension rights and the threat of industrial action as equal causes. I am not satisfied that on a fair reading of his judgment this is what the judge did. The highest that Judge Hellier put it was that a payment can be from employment even though there are other reasons for it: see para [103] of his judgment. This is obviously right. In all the cases I have referred to there are competing causes. Obvious examples are Laidler v Perry (Inspector of Taxes) (1965) 42 TC 351, [1966] AC 16 (staff Christmas bonuses) and Cooper (Surveyor of Taxes) v Blakiston (1908) 5 TC 347, [1909] AC 104 (an incumbent's Easter offerings). In each case the payments were in part motivated by feeling of generosity towards the recipient. Employment does not have to be the sole cause but it does have to be sufficiently substantial as to characterise the payment as one from employment.*

Thus, a payment may be from employment even where there are other competing reasons for the making of the payment.

QC for the Appellant submitted that *Wing v O'Connell* could be distinguished because in that case the payor had never met the jockey whereas Mr. D. gave evidence of his friendship with the Appellant. On day four of the hearing QC for the Appellant submitted:'[Mr. D.] *talks about dedication and commitment, the gratitude of admiration and appreciation for incredibly hard work and dedication over the life of the investment…… Even he talks about the commitment, the incredible leadership. Now in my submission, those are personal qualities; they fit within Herbert v McQuade, they fit within Cowan v Seymour, they fit within these two cases. And it would be wrong in law, in my submission, for you to accept the Revenue Commissioners' submission that it is not possible to have a gift where the gratitude has been generated in respect of services as a blanket proposition, because in my submission, these show that that is possible. And while the personal qualities are lacking in Wing v O'Connell, they're clearly present in this case.'*

Aside from the fact that Mr. D. did not personally make the payment and that the partnerships that discharged the €2.3m to the Appellant were legally incapable of friendship with the Appellant, I do not accept, on the basis of *Wing v O'Connell*, that gratitude and admiration for work done will take a payment beyond the remit of section 112 TCA 1997 in circumstances where the gratitude and admiration are expressly stated to be "*for incredibly hard work and dedication over the life of the investment'*. QC for the Appellant stated that the payment flowed

from gratitude in the first instance however, the gratitude would not have arisen *but for* the work carried out. The gratitude was inextricably linked to the Appellant's work and the payment arose in respect of the work done and thus arose in the context of the employment.

While the payors in this appeal (XYCPGALP and ABFGP) expressed their gratitude to the Appellant for a job well done, their gratitude related directly to the job well done, namely, to the delivery by the Appellant, of the very successful re-flotation of the company in 2007 or, in the words of the payors (as set out in the June 2007 letters) to the delivery of *'the exceptional return that we have achieved to date'.* The gratitude expressed by the payors in relation to work done by the Appellant does not form part of the personal equation and does not present any impediment to characterising the payment as one that arises *from* employment and one that is assessable income tax in accordance with Schedule E.

(iii) Payments by third parties

The payments in this appeal were paid by the shareholders, not by the Appellant's employer, ABG. This was emphasised on behalf of the Appellant in support of his submission that the payment was a gift however, it is a consideration to which I attach minimal weight and the authority for this approach is contained the cases of *Shilton v Wilmshurst* and *O'Connell v Keleghan* [2001] IR 490.

Shilton v Wilmshurst [1991] STC 88, a House of Lords decision, involved the question of taxation of a payment made to a footballer on the occasion of his transfer to a new club. The payment was made, not by his employer, but by a third party. The question which arose was whether the payment was taxable as an emolument arising from employment and the Court held that it was. In that case, Lord Templeman stated;

> *'Section 181 is not confined to 'emoluments from the employer' but embraces all 'emoluments from employment'; the section must therefore comprehend an emolument provided by a third party, a person who is not the employer. Section 181 is not limited to emoluments provided in the course of employment .... an emolument 'from employment' means an emolument 'from being or becoming an employee'. The authorities are consistent with this analysis and are concerned to distinguish in each case between an emolument which is derived 'from being or becoming an employee' on the one hand, and an emolument which is attributable to something else on the other hand, for example, to a desire on the part of the provider of the emolument to relieve distress or to provide assistance to a home buyer.'*

The House of Lords in *Shilton v Wilmshurst* was approved in the Irish Supreme court case of *O'Connell v Keleghan* [2001] IR 490 where the taxpayer received a payment from a company which was not his employer. At page 499 of the report, Murphy J stated;

> *'The unanimous decision of the House of Lords was delivered in the speech of Lord Templeman who noted that the Court of Appeal had accepted that payments made to an employee by a person other than his employer might be liable to tax under sch. E but subject to the qualification that such liability could only arise "where the payer has an interest direct or indirect in the performance of the contract of employment". The House of Lord rejected that qualification pointing out that there was nothing in s 181 of the United Kingdom legislation to justify that inference. I believe that the law so stated in the judgment of Lord Templeman in this respect is a correct statement of the law in this jurisdiction.'*

It is clear therefore, that the source of a payment need not be the employer, nor must the payor have a direct or indirect interest in the performance of the contract of employment. However, the payors in this appeal (XYCPGALP and ABFGP) had a clear interest in the performance of the Appellant. The letters sent by them on 14 and 29 June 2007 stated that the payors were '*.... conscious of the sacrifices that you made in this period of your life to deliver the exceptional return that we have received to date...'* .

In addition, during re-examination of Mr. D. by QC for the Appellant, Mr. D. was asked what he meant by the reference to '*sacrifices'* in the letter and Mr. D. responded;

> *'.. what I am referring to there is what I mentioned earlier which is in my 36 years in this business I have never seen a chief executive officer work as hard as Mr. C. with as much commitment... My partners at XY were aware of that. You know Mr. C. works..., worked non-stop, weekends, you name it, he was working. It was beyond anything I had ever seen. It was beyond anything that Mr. E. or Mr. K. had ever seen. It was extraordinary, it was extraordinary. It was incredible leadership for the organisation and it's really that extraordinary leadership that we felt to grateful for. That's what I am getting at in that letter.'*

Thus a payment may be from employment notwithstanding that it was *not* paid by the Appellant's employer and such circumstances present no impediment to characterising the payment as one that is assessable to income tax in accordance with Schedule E.

(iv) Labels attributed to the payment

As stated above, labels given to the payment by the parties are not determinative of the character of the payment. In this regard, the use of the words 'award' and 'awarded' in the Annual Report are significant and are at odds with the reference to 'gift' in each of the letters from XYCPGALP and ABFGP in June 2007. Equally in *Wing v O'Connell*, the payment was taxed as an emolument notwithstanding the fact that the payment was described as a '*present'*.

(v) Motivation

The intention or motivation of the payor is not determinative of the nature or character of that payment for tax purposes and this principle is supported by the dicta of Fitzgibbon J. in *Wing v O'Connell* where at page 108, he quoted the following from *Cooper v Blakiston; 'The question is not what was the motive of the payment, but what was the character in which the recipient received it?*

(vi) Divergence in Irish and UK law

As set out above, in accordance with *Wing v O'Connell*, it matters not that the payment made was spontaneous, unexpected or voluntary. The Appellant sought to rely on the UK First Tier Tribunal case of *Colin Collins v Revenue Customs Commissioners* [2012] UKFTT 411 where the '*gratuitous and unexpected*' nature of the payment was taken into consideration.

The *Collins* case can be distinguished from the within appeal on a number of grounds including; that the Appellant in that case had ceased to work four years prior to receiving the payment, that the donor in that case had sold the company eighteen months prior to making the payment and that the sum received by the Appellant in that case was described at page 20 of the report as being '*wholly disproportionate to the amount of the Appellant's past salary*' whereas the €2.3m paid to the Appellant was not disproportional to his salary, rather, it was twice his salary.

The Appellant also placed reliance on the case of *Kieran Anthony Rogers* [2011] UKFTT 167, a case which related to the transfer of shares worth €2.8m which took into consideration, factors which are not relevant in Irish jurisprudential analysis, such as; whether the payment was recurrent or once-off, whether the value of the receipt is large in relation to the employee's ordinary salary, whether the taxpayer was paid a market rate salary (and whether an additional payment is less likely to be remuneration) whether the employee has a contractual entitlement to receive the payment or benefit and whether there is an inference

that the payment is less likely to be an emolument if it is paid by a person other then the employer.

It should be noted that both the *Collins* case and the *Rogers* case are decisions of the First-tier Tribunal and do not appear to have been appealed.

In the Irish Supreme Court case of *Wing v O'Connell*, the fact that the payment was gratuitous (i.e. there was no consideration for it) or that it was unexpected (insofar as it was in excess of the remuneration to which the jockey was entitled) or that it was voluntary, did not affect the application of the income tax statute and did not affect the conclusion that the '*present*' of £400 was an emolument assessable to income tax.

The Appellant also relied on *Bridges v Bearsley* (1957) 37 TC 289, a case which is very particular on its facts and which does not accord with the Irish cases of *Wing v O'Connell* or *O'Connell v Keleghan* [2001] IR 490. The *Bearsley* case concerned the question of compensating the respondents for not having been provided for in the will of the principal shareholder on foot of assurances they had received from him during his life time. It is a case which stands very much upon its own facts.

(vii) Whether the payment was a payment on termination of employment

The payment received by the Appellant in this case was not a payment on the cessation or termination of employment and this was clear from the evidence.

In his witness statement, the Appellant stated; *'I did not at any point think that the gift was intended to be some sort of sweetener, or a way of locking us into the company. No-one was thinking of leaving. We were all highly motivated and very well paid*.'

On the first day of the hearing the Appellant in his evidence discussed how he would have to hold his shares for several years after the IPO because: *'… it's not well received by shareholders to see the CEO of a plc selling shares. And so therefore, other than very specific circumstances, the … normal expectation is that CEOs would hold their shares, generally speaking until they retire or leave the company.'*

Further, at paragraph 44 of his witness statement, the Appellant stated; '*Had it not been the case that the senior management in* [ZA Group] *and subsequently ABG were long term in their service and approach, there would be evidence of executives playing the cycle and earnings*

potential, as I have witnessed in other businesses, namely exiting the business at the point of a major share and the peak of a particular cycle.'

I am satisfied that payment received by the Appellant in this appeal was not a payment on the cessation or termination of employment and the case law in relation to termination payments, including *Mulvey v Coffey* (1942) IR 277 upon which the Appellant relied, are not relevant in ascertaining the character of this payment for tax purposes.

Conclusion

Section 112 sets out the basis of assessment and extent of the charge to tax under Schedule E which arises *'...in respect of all salaries, fees, wages, perquisites or profits whatever therefrom...'.*

In *Tennant v Smith* (1892) 3 TC 158, Lord Watson stated that *'in order to make a thing an emolument, it must be something either in money or capable of being converted into money'.* He also stated: *'.... To be a perquisite or emolument, it must be money or money's worth'.* I am satisfied that the payment of €2.3m in this appeal falls within '*salaries, fees, wages, perquisites or profits whatever'* in section 112 TCA 1997.

At the core of the dispute in this appeal is the question of whether the payment of €2.3m to the Appellant by the shareholders arose from his employment or whether it was made for personal reasons forming part of the personal equation or whether it arose from something else.

The Appellant in his evidence and in the evidence of the witnesses he called and in the submissions he lead through his QC, emphasised that the payment was received by him for reasons of gratitude, admiration, respect and appreciation.

Section 112 taxes emoluments arising from employment and the Appellant argued that the qualities of gratitude, admiration, respect and appreciation were personal qualities which lifted the payment out of the remit of section 112 and into the realm of the personal equation. This is fundamentally incorrect. One simply cannot separate the success from the employment and characterise it as a personal quality separate to the employment. Irish jurisprudence which has tested and measured the scope of section 112 and its equivalents over the past one hundred years supports no such proposition.

On the contrary, the Supreme Court authority of *Wing v O'Connell* per the dicta of Kennedy C.J. provides: '*there is .... no foundation in fact for the attempt to separate the success as something purely personal from the riding, which is admittedly professional*.'

The payment made to the Appellant was not made on grounds of compassion, altruism, ill-health, indigence or other similar reasons. Nor was the payment made from 'something else' per the dicta of Lord Reid in *Laidler v Perry*. Further, the payment was not a singular award made to the Appellant, but one of four awards made to the entire senior management team. This undermines considerably, the submission that the payments were made for reasons personal to the Appellant. The payment to the Appellant did not form part of the personal equation, which leads to the question: *what were the payments for?*

In truth, what this payment represented was a payment in respect of the very extensive amount of work undertaken by Mr. C. in the five-year period prior to the IPO in 2007. The letters issued to the Appellant in June 2007 referred to "*your efforts and commitment throughout the period of our investment in the AB Group".* The payment reflected not just the successful completion of the IPO but also the significant growth of the company between 2002 and 2005, when, as paraphrased above, the 2007 annual report provides that; *in difficult market conditions, immense progress was made.*

The timing of the making of the payment in 2011 coincided with the realisation of the shareholder profits.

The payment, which was in addition to the Appellant's remuneration, related to his extraordinary dedication and effort as opposed to being for that fact that he merely held a position in the company. It is clear from the evidence that payments of this nature were rare across the industry as a whole. It was unusual for an employee in this field to be rewarded financially outside of their contractually agreed remuneration, and in particular to be rewarded so significantly. It suggests that the Appellant went far beyond what was expected or what one might normally see in terms of his performance in relation to his employment.

In conclusion, I am satisfied that the payments received by Mr. C. were for the exceptional services rendered by Mr. C. which contributed significantly to the increase in value of the shares of the private equity firms who were the principal shareholders in ABG and who generated a return on their investments in the region of US$350 million. It is not possible to separate Mr. C.'s individual excellence, from his role as CEO in circumstances where the

means of demonstrating his excellence was by being CEO, by acting as CEO and by delivering exemplary results as CEO.

The burden of proof

In appeals before the Tax Appeals Commission, the burden of proof rests on the Appellant who must prove on the balance of probabilities that the assessments are incorrect. This accords with the general law in civil cases that the burden of proof falls on he who asserts.

In the High Court case of *Menolly Homes Ltd v Appeal Commissioners and another,* [2010] IEHC 49, at para. 22, Charleton J. stated:

'The burden of proof in this appeal process is, as in all taxation appeals, on the taxpayer. This is not a plenary civil hearing. It is an enquiry by the Appeal Commissioners as to whether the taxpayer has shown that the relevant tax is not payable.'

In this appeal, the Appellant set out to establish that the payment arose from something other than his employment. Having considered the evidence and facts, the relevant legislation and related case law, I determine that the Appellant did not succeed in demonstrating that the payment arose from a source other than the employment and I determine that the Appellant has not discharged the burden of proof in this appeal

Determination

I determine that the payment of €2.3 million made to the Appellant constitutes a taxable emolument assessable to income tax in accordance with section 112 TCA 1997.

I determine that the notice of amended assessment for the year ending 31 December 2007 assessment shall be adjusted as follows;

- That part of the assessment which shows on the assessment a sum of €5,438,077, taxable in accordance with Schedule E (which sum includes the sum of €2.3m euros paid to the Appellant) shall stand, on the basis that the sum of €2.3m received by the Appellant from the shareholders constitutes a taxable emolument assessable to income tax in accordance with section 112 TCA 1997.

- On page 3 of the assessment, that part of the assessment which shows on the assessment a sum of €2,300,176 taxable in accordance with Schedule D (which sum includes the sum of €2.3m euros paid to the Appellant) shall be reduced to one hundred and seventy-six euros, taxable in accordance with Schedule D.

A separate assessment was raised in respect of the year ending 31 December 2011. As regards this notice of amended assessment, I determine that the payment of €2.3m where it appears on this assessment, shall be reduced to zero and the assessment discharged.

This appeal is hereby determined in accordance with s.949AK TCA 1997.

COMMISSIONER LORNA GALLAGHER

June 2019

The Tax Appeals Commission has been requested to state and sign a case for the opinion of the High Court in respect of this determination, pursuant to the provisions of Chapter 6 of Part 40A of the Taxes Consolidation Act 1997 as amended.