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CURRENT DEVELOPMENTS: CASE COMMENT

Beneficial ownership in domestic tax legislation, some clarity, but far from 'well established': *Hargreaves Property Holdings Ltd v HMRC* [2024] EWCA Civ 365

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The concept of beneficial ownership is extensively used in domestic tax legislation, but several decades of inconsistent case law have muddied the waters as to exactly what it means. With the leading cases stopping short of the apex court, it is difficult to reconcile the cases and come up with a clear definition of beneficial ownership. The recent *Hargreaves*[1] decision by Falk LJ (with whom Nugee and Peter Jackson LJJ agreed) represents the most structured judicial attempt to rationalise the concept to date. This note suggests that, contrary to Falk LJ's statement that the concept is 'well established',[2] the law pre-*Hargreaves* was far from clear. This situation has since been greatly improved through the efforts of Falk LJ, though further questions remain for future judicial clarification.

In *Hargreaves*, the court had to determine whether a recipient (Houmet) of interest payments made by the appellant (Hargreaves), was 'beneficially entitled' to the payments. If so, Hargreaves could avail itself of an exception to the requirement to deduct and account for withholding tax on such interest. Hargreaves periodically borrowed money from creditors, who would sell and assign their rights to the interest payments to Houmet. The Court found that the sole purpose of Houmet's involvement in the transactions was to give Hargreaves the tax advantage of not having to deduct and account for withholding tax. It held that Hargreaves had not discharged its burden of proof of showing that Houmet had any of the benefits of being entitled to or receiving the interest payments and thus, was not 'beneficially entitled' under the statute. Houmet's involvement not only had no commercial purpose but also no practical or real effect.

The case provided the court with an opportunity to review the existing law on beneficial ownership, which it recognised should be considered when looking at the related concept of beneficial entitlement. One of the long-standing questions on beneficial ownership has to do with the way that the concept may differ when used in different contexts. Falk LJ recognised that the 'international fiscal meaning' of beneficial ownership as laid out in *Indofood*[3] differed from the position in relation to 'domestic tax legislation' that applied in the present case.[4] Indeed, while the term 'beneficial ownership' is used across many areas of (tax) law, the concepts vary considerably depending on the context and only share similarities at a very high level of abstraction. Beneficial ownership in the context of domestic tax

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[1] *Hargreaves Property Holdings Ltd v HMRC* [2024] EWCA Civ 365 (*Hargreaves*).

[2] Ibid, at [31] and [49]; and *J Sainsbury plc v O'Connor* [1991] 1 WLR 963 (CA) at 969 per Lloyd LJ (*Sainsbury*).

[3] *Indofood International Finance v JP Morgan Chase Bank* [2006] EWCA Civ 158 (*Indofood*).

[4] *Hargreaves*, above n 1, [56].

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legislation has its roots in the law of equity,[5] unlike the concept as applied in tax treaties in the international tax context, which has its own distinct history and use.

Historically, equity and the common law were distinct branches of the law that were administered by separate courts. Even though the Judicature Act 1873 fused the administration of both branches of law, their legal principles remain conceptually distinct.[6] Legal concepts derived from the law of equity must be understood in light of the history and body of case law from which they developed. As domestic tax law statutes have never sought to define beneficial ownership, the courts have always made it clear that the concept is to be drawn from the equitable case law.[7] This stands in stark contrast to the 'international fiscal meaning' of beneficial ownership, which started to become more widespread when the term was first used in the OECD Model Convention in 1977. Subsequent case law and guidance has made it clear that the 'international fiscal meaning' of beneficial ownership is not the same as the domestic tax law meaning,[8] which is in line with the fact that numerous treaty states do not recognise the law of equity in their domestic law. When beneficial ownership was adopted as a concept in international tax law, it was severed from its equitable roots and came into its own as a distinct concept.

Falk LJ's clarification was particularly welcome because when the *Hargreaves* case was considered by the Upper Tribunal,[9] there was some confusion as to whether the Tribunal applied the 'international fiscal meaning' of beneficial ownership.[10] The Tribunal held that the exception was 'for the benefit of UK companies who are substantively entitled to receive and enjoy the income'.[11] This language here is very similar to that used by the Court of Appeal in *Indofood*,[12] where the court held that 'the concept of beneficial ownership is incompatible with that of the formal owner who does not have "the full privilege to directly benefit from the income"'.[13] The decision of the Upper Tribunal thus increased the risk that the two distinct concepts of beneficial ownership would be conflated and applied in an inappropriate context. Falk LJ's judgment now makes it clear that the 'international fiscal meaning' of beneficial ownership is to be rejected in the context of applying 'domestic tax legislation'.

With the expansion of the use of the term 'beneficial ownership' in various other statutes, the risk of conflation is greater than ever. The global shift towards transparency and exchange of information for tax and anti-money laundering purposes has resulted in beneficial ownership and the related concept of 'controlling persons' being used in a wide variety of initiatives such as the Common Reporting Standard and Foreign Account Tax Compliance Act.[14] Yet, the concept of beneficial ownership used in these contexts bears little relation to the concept as used in domestic tax law (or the 'international fiscal meaning'). This is of particular concern as the international 'exchange of information' concept of beneficial ownership makes its way back into UK legislation in the form of statutes such as the Economic Crime (Transparency and Enforcement) Act 2022.

Falk LJ laid out six other principles, starting with the idea that beneficial ownership, in essence, means ownership for the benefit of the person in question.[15] In doing so, she cited[16] Nourse LJ's definition in *Sainsbury* as 'ownership for your own benefit as opposed to ownership as trustee for another', existing regardless of whether there is a division of legal and beneficial ownership (or there is an 'undivided whole').[17] Falk LJ also made it clear that the fact that the concept of beneficial ownership is well

[5] *Ayerst v C & K (Construction) Ltd* [1976] AC 167 (HL) at 177–178 per Lord Diplock (*Ayerst*).
[6] J Glister and J Lee *Hanbury & Martin: Modern Equity* (Sweet & Maxwell, 23rd edn, 2024) 1-020.
[7] *Ayerst*, above n 5, at 177 per Lord Diplock.
[8] *Indofood*, above n 3, at [42] and the OECD Model Commentary (2014), Art 10, para 12.6.
[9] *Hargreaves Property Holdings Ltd v HMRC* [2023] UKUT 00120 (TCC) (*Hargreaves (UT)*).
[10] D Robertson 'Beneficial entitlement in *Hargreaves*: is *Indofood* now part of UK domestic law?' (7 July 2023) Tax Journal 10.
[11] *Hargreaves (UT)*, above n 9, [29].
[12] Robertson, above n 10, at 11.
[13] *Indofood*, above n 3, at [42].
[14] See for example X Oberson *International Exchange of Information in Tax Matters* (Edward Elgar, 3rd edn, 2023.
[15] *Hargreaves*, above n 1, at [49].
[16] Ibid, at [43].
[17] *Sainsbury*, above n 2, at 978 per Nourse LJ, citing *Ayerst*, above n 5, at 177 per Lord Diplock.

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established does not mean that usual approach to statutory construction is to be ignored. Applying *Hurstwood*,[18] she emphasised that there is no 'special category of statutory concept that is immune from purposive construction'.[19] In fact, it might be argued that because the concept of 'ownership' is a complex one often subject to multiple interpretations,[20] it is all the more important to discern Parliament's intention in relation to that particular statutory provision.

In *Parway Estates*, the court arguably equated beneficial ownership with equitable ownership.[21] However, in *Wood Preservation*, Lord Donovan drew a distinction between the two concepts.[22] This was done without reference to *Parway Estates*, despite the express consideration by Goff J in the High Court.[23] Subsequently, in *Sainsbury*, the court felt bound by *Wood Preservation*, despite Lloyd and Nourse LJJ strongly indicating that they would have preferred to follow *Parway Estates.*[24] In *Hargreaves*, Falk LJ acknowledged that it was unclear on what basis *Parway Estates* could be distinguished from *Wood Preservation*, but stopped short of declaring that *Wood Preservation* and *Sainsbury* were thus decided *per incuriam*, since *Parway Estates* would technically be binding in both cases. She attempted to rationalise the cases by holding that *Parway Estates* had laid out the proposition that a purchaser under a specifically enforceable contract can (but need not always) have beneficial ownership of the asset under the contract.[25]

Falk LJ held that while beneficial ownership and equitable ownership are not entirely co-extensive, there is a significant degree of overlap between the concepts.[26] She suggested that one reason might be to allow the former concept to operate in legal systems that do not have the same legal traditions, such as Scotland.[27] Falk LJ further considered that 'beneficially entitled' must mean 'entitlement with benefits', conferring some 'real and practical entitlement', 'which carries at least some of the benefits of ownership' and not merely 'equitable ownership'.[28] This is in line with Lord Diplock's reference in *Ayerst* to 'ownership for your own benefit'.[29] It is noted that the prefix 'equitable' arguably only means that the root term is 'enforced by equity', whereas 'beneficial' connotes some right to enjoy for one's own benefit. As such, beneficial ownership should be seen as a subset of equitable ownership, since it is a necessary but insufficient condition for a right to be 'enforced by equity' in order to be beneficial. In equating the two concepts, *Parway Estates* would appear to be incorrectly decided and Falk LJ's approach in *Hargreaves* provides an opportunity to untangle the mess of inconsistent case law on this issue.

This difference between the prefix 'equitable' and 'beneficial' is also useful when looking at the decision of the Upper Tribunal in *Hargreaves*, where it held that the exception was 'for the benefit of UK companies who are substantively entitled to receive and enjoy the income' and 'not those who are beneficially entitled only in the narrower technical sense used to distinguish between legal and equitable interests in English common law'.[30] Indeed, merely having the equitable interest would not render one beneficially entitled. There must also be some right to enjoy for one's own benefit. However, it would be inappropriate to bring in the concept of 'substantive entitlement to receive and enjoy the income' from the 'international fiscal meaning' of beneficial ownership in this context.

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[18] *Rossendale BC v Hurstwood Properties (A) Ltd* [2021] UKSC 16. See V Ooi 'At the intersection of artificiality, forward piercing not allowed' (2025) 36(1) King's Law Journal 1.

[19] *Hargreaves*, above n 1, at [30].

[20] A Honoré 'Ownership' in P Smith (ed) *The Nature and Process of Law: An Introduction to Legal Philosophy* (Oxford University Press, 1993) p 370.

[21] *Parway Estates v IRC* (1957) 45 TC 135 (CA) at 148 per Jenkins LJ.

[22] *Wood Preservation v Prior* [1969] 1 WLR 1077 (CA) at 1096 per Lord Donovan (*Wood Preservation*).

[23] Ibid, at 1094 per Goff J.

[24] *Sainsbury*, above n 2, at 975 per Lloyd LJ and 979 per Nourse LJ.

[25] *Hargreaves*, above n 1, at [50].

[26] Ibid.

[27] Ibid.

[28] Ibid, at [65].

[29] *Ayerst*, above n 5, at 177 per Lord Diplock.

[30] *Hargreaves (UT)*, above n 9, at [29].

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In *Hargreaves*, Falk LJ observed that beneficial entitlement should be construed with regard to the authorities that consider beneficial ownership.[31] Indeed, insofar as the common prefix of the terms falls to be interpreted, the two concepts are similar. However, while the court expressly noted a difference between ownership and entitlement there was perhaps a missed opportunity to explore this area further. In addition to the two, the terms 'interest' and 'enjoyment' are also commonly prefixed by 'beneficial' or 'equitable'. The four terms all describe various rights held by a person and are commonly used in domestic tax statutes.[32] Ownership is perhaps the most narrowly defined term and there will be many more situations where a person may be said to be beneficially entitled to an asset than said to be the beneficial owner. 'Entitlement' appears to be broad and capable of encompassing any legal right or collection of rights, prospective or otherwise, whereas 'ownership' generally requires one to have 'the greatest interest in a thing'.[33] In domestic tax law, while there can be many who are entitled to an asset, there can generally only be one owner. While *Hargreaves* acknowledges the importance of the case law on beneficial ownership in determining beneficial entitlement, the differences as well as the similarities of the terms should be considered.

Another missed opportunity by the court in *Hargreaves* was the failure to decisively reject the misguided 'mere legal shell' test. As Falk LJ noted,[34] the term was first introduced by Harman LJ in *Wood Preservation*, who held that as the legal owner in that case was not able to deal with the property in any way at all, there was no benefit at all in their ownership, being a mere legal shell.[35] A careful reading of *Wood Preservation* makes it clear that Harman LJ did not intend this to be a test, but rather a conclusion on the facts of the case before him. The same can be said when Lloyd LJ used the same term in *Sainsbury*.[36] However, subsequent commentators and cases have misinterpreted the 'mere legal shell' test. A case note published shortly after *Sainsbury* was decided submitted that the impact of the judgment is that 'it is only where the rights retained by the shareholder are "a mere legal shell" that beneficial ownership has been lost'.[37] The commentator went on to state that 'if the rights retained are more than "a mere legal shell," and equitable ownership has not passed, beneficial ownership is likely to be retained'.[38]

The Upper Tribunal in *Bupa Insurance* proceeded along similar lines, holding that 'any incidents of ownership which amount to more than a "mere legal shell" amount … to "beneficial ownership"' and that 'the legal owner must be bereft of "all rights which would normally attach to [the asset]" to be deprived of beneficial ownership of the asset'.[39] Such interpretations of Harman LJ's judgment (erroneously) turn his conclusion on the facts before him into a test and go much further than what he was saying. The 'mere legal shell test' as stated in *Bupa Insurance* places an unwarranted emphasis on the legal owner (as opposed to any other person with equitable rights in a thing) and is at odds with the traditional understanding that the owner is the holder of the greatest interest in a thing.[40]

Falk LJ in *Hargreaves* did not make the same error, holding that a person who is the legal owner of the property will not be its beneficial owner if they do not in fact have any of the benefits of ownership, such that they hold only a 'mere legal shell'.[41] It is indeed correct to say that the holder of a 'mere legal shell' cannot be the beneficial owner, though the statement is perhaps of somewhat limited utility, since it does not tell us what the test for determining the beneficial owner is. However, having cited and considered *Bupa Insurance*, the court might have taken the chance to reject the 'mere legal shell test' once and for all.

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[31] *Hargreaves*, above n 1, at [54].

[32] See V Ooi 'The shift from an inclusionary to an exclusionary focus: the relatively late appearance of beneficial ownership in UK tax statutes' in P Harris and D de Cogan (eds) *Studies in the History of Tax Law*, Volume 12 (Hart Publishing, forthcoming).

[33] Honoré, above n 20, p 370.

[34] *Hargreaves*, above n 1, at [36].

[35] *Wood Preservation*, above n 22, at 1096–1097 per Harman LJ.

[36] *Sainsbury*, above n 2, at 976, per Lloyd LJ.

[37] T Scott 'Group therapy' (1991) British Tax Review 229 at 232.

[38] Ibid, at 233.

[39] *Bupa Insurance Ltd v HMRC* [2014] UKUT 262 at [59] and [60].

[40] Honoré, above n 20, p 370.

[41] *Hargreaves*, above n 1, at [52].

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Finally, citing *Ayerst*,[42] Falk LJ held that in certain circumstances, it is possible for a property owner not to possess, or to lose, beneficial ownership without it vesting anywhere else.[43] However, this should not be overstated. It is noted that the examples given in *Ayerst* involve an estate being administered and a statutory winding-up scheme.[44] These are far from common cases and *Jerome v Kelly* suggests that in a standard contractual case, the beneficial ownership will not be in suspense at any point in time during the transaction.[45]

It is worth noting that Falk LJ did not identify which party was 'beneficially entitled' to the payments, but instead decided the case on the basis that Hargreaves had not discharged its burden of proof of showing that Houmet had any of the benefits of being entitled to or receiving the interest payments and thus, was not 'beneficially entitled' under the statute. This may have implications for subsequent courts attempting to determine the *ratio decidendi* of this decision. While Falk LJ has certainly provided valuable guidance on beneficial ownership in the context of domestic tax legislation, it is arguable that much of this might technically be *obiter dicta*.

That said, *Hargreaves* provides an excellent structure for thinking about the concept of beneficial ownership. Many previously ambiguous points have also been clarified. It is now clear that general principles of purposive interpretation are to be applied to beneficial ownership; that there is a significant degree of overlap between beneficial ownership and equitable ownership, but that the concepts are not the same. Further, we have some guidance on the test to be applied to determine beneficial entitlement (which may be extended to beneficial ownership). Falk LJ held that 'beneficially entitled' must mean 'entitlement with benefits', conferring some 'real and practical entitlement', 'which carries at least some of the benefits of ownership' and not merely 'equitable ownership'.[46] This is useful guidance that will no doubt form part of the core jurisprudence of the concept and be applied in future cases. However, it is a pity that the opportunity to definitively put the 'mere legal shell test' to rest was not taken in this case. By referencing the 'test' without rejecting it, there is a risk that this case will be interpreted as supporting the formulation in *Bupa Insurance*, perpetuating the erroneous application of this 'test' to determine beneficial ownership.

[42] *Ayerst*, above n 5, at 178 per Lord Diplock.
[43] *Hargreaves*, above n 1, at [53].
[44] *Ayerst*, above n 5, at 178 per Lord Diplock.
[45] *Jerome v Kelly (Inspector of Taxes)* [2004] STC 887 (HL) at [32] per Lord Walker.
[46] *Hargreaves*, above n 1, at [65].

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