# ‘The normal meaning of securities is not open to doubt’. Lord Cave in *Singer v Williams* (1920). Is that right?

Victor Baker\*

## Introduction

*The normal meaning of securities is not open to doubt*. Thus spoke Lord Cave in *Singer v Williams*[[1]](#footnote-1) in 1920. In that case, the appellant, who resided in England and was a shareholder in the Singer[[2]](#footnote-2) Manufacturing Company of New Jersey, claimed in respect of his income therefrom to be assessed upon the dividends received during the last financial year and not upon the average dividends of the preceding three years. Held that such income was derived from foreign possessions under Case V of Schedule D and not from foreign securities under Case IV, so the tax was computed on the three years’ average basis, according to the legislation of the time.[[3]](#footnote-3)

This paper takes that statement as its starting point and examines tax case law on the meaning of securities and uses that as a springboard to examine how the wider meaning of ‘security’ and ‘securities’ originated and developed its tax meaning, the importance of the concept of securities and its relation to shares, and how the tax meaning of securities compares with the wider commercial usage of the word, extending to the important contemporary question of what security tokens are in the context of the regulation and taxation of cryptographic assets or ‘crypto’.

This paper is divided into five parts. Part 1 looks at the tax definitions and case law on the meaning of securities, and in particular at the speeches of the Law Lords in *Singer v Williams*. Part 2 looks at the wider meaning of security and securities and how that meaning has developed towards its application in tax law. Part 3 considers the important distinction between shares and securities in the context of the corporation tax distributions legislation and the related question of equity and loan capital in establishing group relationships. Part 4 considers the meaning of securities in commerce and economics, where the concepts of shares and securities are often not distinguished, and the differences in tax treatment of returns on shares and securities are regarded by many as undesirable and economically distorting. Part 5 looks at the contemporary challenges around security tokens in the cryptoassets field.

## Tax definitions and case law on the meaning of securities

There are many definitions cited in tax statutes, but mostly they include shares in companies, or sometimes explicitly exclude them but include loan stock and similar, or are comprehensive of shares, stocks, bonds and debentures. The definition for the purposes of distributions by a company includes securities which do not create or evidence a charge, and even loans not made on the issue of securities ‘or other consideration given by the company’; here in effect securities are implied into a loan arrangement. There is no definition in Schedule 1 to the Interpretation Act 1978. There are definitions in some non-tax legislation and regulatory practice, for example section 4 of the Stock Transfer Act 1963, as amended by the Financial Services and Markets Act 2000 (FSMA 2000), defines securities as meaning shares, stock, debentures, debenture stock, loan stock, bonds, units of a collective investment scheme within the meaning of FSMA 2000, ‘and other securities of any description’. This is an area where definitions differ according to purpose and context, and care must be exercised accordingly[[4]](#footnote-4).

#### Tax definitions

The main definitions are for the purposes of chargeable gains, company distributions, the transactions in securities anti-avoidance legislation and stamp taxes but there are other specific usages, for example in the employment-related securities legislation (section 420 Income Tax (Earnings and Pensions) Act 2003).

Section 132 of the Taxation of Chargeable Gains Act 1992 provides that ‘security’ includes any loan stock or similar security whether of the government of the United Kingdom or of any other government, or of any public or local authority in the United Kingdom or elsewhere, or of any company, and whether secured or unsecured.

The company distributions legislation at section 1117(1) of the Corporation Tax Act 2010 (CTA 2010) defines ‘security’, except where the context otherwise requires, as including securities not creating or evidencing a charge on assets, and at section 1114(3) contains, for the purposes of company distributions, the formula mentioned above that treats interest paid by a company on advances to it as paid in respect of a security issued by it without the actual issue of a security or other consideration given by the company.

The transactions in securities legislation, which originated in Finance Act 1960 (FA 1960) to deal with ‘dividend stripping’ and ‘bond washing’ and is now at Part 15 of CTA 2010 (sections 731 to 751), defines for that purpose at section 751 securities as including shares and stock, and in relation to a company not limited by shares (whether or not it has a share capital) includes a reference to the interest of a member in the company as such, regardless of the form of interest.

In the analogous income tax provisions[[5]](#footnote-5) there is no definition of securities, only one of transactions in securities, which is a transaction, of whatever description, relating to securities. Not greatly illuminating.

The Stamp Act 1891 with similar lack of illumination provides a definition for ‘marketable security’, which means a security of such a description as to be capable of being sold in any stock market in the United Kingdom.

#### Speeches in Singer v Williams

Lord Cave said

… the normal meaning of ‘securities’ is not open to doubt. The word denotes a debt or claim the payment of which is in some way secured. The security would generally consist of a right to resort to some fund or property for payment. But I am not prepared to say that other forms of security (such as personal guarantees) are excluded. In each case, however, where the word is used in its normal sense, some form of secured liability is postulated. No doubt the meaning of the word may be enlarged by an interpretation contained in a statute … or the context. But in the absence of such aid to interpretation, I think it is clear the word ‘securities’ must be construed in the sense above defined, and accordingly does not include shares or stocks in a company.

As we shall see, that type of personal guarantee is one established meaning of security.

Lord Atkinson described the extension of securities to include shares as sometimes reflected in ‘popular language’ but noted that shares are portions of the capital of a company and are choses in action only in that they are assignable and any assignee would be entitled to sue to obtain his share of the profits as the original holders would be.

Lord Shaw observed that ‘possession’ is a term of wide meaning and would cover ‘securities’ too, but in context the statute construed foreign possessions and foreign securities differently, placing the latter in a different category. He said:

‘Securities’ is an ordinary English word without legal definition and must be construed in context. Here there is a security upon something, distinct from the lodging of a security or securities with a bank. It invokes the relationship of debtor and creditor, but Mr Singer is a shareholder, a joint adventurer with others, a part owner. The variability of ownership returns is recognised by the three-year average basis which applies to possessions but not securities.

Lord Wrenbury adopted an interesting analysis which perhaps deserves to be better known. That a security is a possession, but such that the grantee or holder of the security holds as against the grantor a right to resort to some property or some fund for the satisfaction of some demand, after whose satisfaction the balance of the property or fund belongs to the grantor. He went on to say:

There are two owners, and the right of the one has precedence of the right of the other. A share in a corporation does not answer the above description. There are not two owners, the one entitled to a security upon something and the other entitled to the balance after satisfying that demand. A share confers upon the holder a right to a proportionate part of the assets of the corporation; it may be a proportionate part of its profits by way of dividend, or it may be a proportionate part of its distributive assets in liquidation. There is no owner other than himself.

Lord Phillimore was less certain than his brethren, but he too recognised a ‘strict sense’ of the word securities, and a wider ‘popular’ sense extending to stocks and shares. He thought[[6]](#footnote-6) that possessions generally connote something tangible, like a sugar plantation, and that choses in possession might be distinguished from choses in action. But there was high authority for considering foreign possessions as including any form of property from which profit may be derived, and that the likely explanation for the language was that in 1842[[7]](#footnote-7) there were few incorporated companies, and fewer still that were foreign resident and owned by British shareholders, that what was principally in mind was lands, plantations and factories abroad, but the language was wide enough to include all foreign species of property. Lord Phillimore was swayed by the reference not so much to securities as to the fact that the charge was on *interest* arising from them. The word securities was therefore being used in the ‘narrower and technical sense’.

This conclusion is consistent with the historical definitions of Case IV and Case V originating in Addington’s Act of 1803. The following is taken from the Act of 1806.[[8]](#footnote-8)

*Schedule D Fourth Case*. The Duty is to be charged in respect of Interest arising from Securities in Ireland, or in the British Plantations in America, or in any of his Majesty’s Dominions out of Great Britain and Foreign Securities, except such Dividends and Annuities and Shares, payable out of the Revenue of Ireland, as are directed to be charged under Schedule (C) of this Act.

*Schedule D Fifth Case*. The Duty is to be charged in respect of possessions in Ireland, or in the British Plantations in America, or in any other of His Majesty’s Dominions out of Great Britain, and Foreign Possessions.

We can see here the differences subsequently brought out in the speeches in *Singer v Williams* above. Interest, within Case IV, is a return which arises and is payable on an advance in relation to a principal fund which is secured under specified terms of an agreement, while Case V is charged in respect of ‘possessions’ which will include dividends which are a part realisation of the possessions, the equity interests or shares in the company.

#### Other case law

There is an early stamp duty case *Brown, Shipley & Co v Inland Revenue Commissioners[[9]](#footnote-9)* which considered the meaning of ‘marketable security’. A secured promissory note issued by a railway company, whose security consisted of a deposit of gold bonds held on trust for the holder, was considered by Lord Esher to be a security on the ground that there was a promise that the holder of the note ‘shall have the security’, the benefit of the gold bonds. It was the availability of the collateral against the loan that made the promissory note a ‘security’ in this context.

In *Cleveleys Investment Trust Co v Inland Revenue Commissioners (No.1)[[10]](#footnote-10)* the issue was ‘debt on a security’, but the meaning of security itself was also considered. The appeal tribunal (the Special Commissioners) interpreted ‘security’ in this context as a right to secure payment by reference to some property or fund other than a right *in personam* against the debtor. On the particular facts under consideration the Special Commissioners decided that neither of the documents examined, a letter of understanding and a bill of exchange, amounted to a security. Lord Migdale in the Court of Session (First Division), in a dissenting judgment, said he did not wholly agree with the Commissioners’ reasoning while agreeing with their conclusion. He went on:

The word ‘security’ has two meanings. It may refer to some property deposited or made over or some obligation entered into by or on behalf of a person in order to secure his fulfilment of an obligation he has undertaken. Or it may refer to a document held by a creditor as evidence or a guarantee of his right to repayment. (See *Shorter Oxford English Dictionary*, vol. 2.) I think that the words ‘the debt on a security’ refer to an obligation to pay or repay embodied in a share or stock certificate issued by a government, local authority or company which is evidence of the ownership of the share or stock and so of the right to receive payment. This reading of this section enables me to give some effect to the words ‘whether secured or unsecured’.

In *WT Ramsay Ltd v Inland Revenue Commissioners*[[11]](#footnote-11) it was held that, as respects a debt on a security, marketability, the characteristic of being capable of being realised, or dealt with at a profit, was of the essence. Lord Wilberforce observed that a debt, to qualify as a debt on a security, need not necessarily be constituted or evidenced by a document. Its existence may be an indicative factor, but its absence is not fatal.[[12]](#footnote-12)

In *Shaw v Samuel Monatagu & Co Ltd*[[13]](#footnote-13) the Special Commissioner considered whether the company’s holdings of metals were securities. He said:

Everyday usage has widened the meaning of the word ‘securities’ significantly since 1921, but in 1959 *Vaisey* J did not find it difficult to determine what was not included within the definition of that word. He said, in *Re Douglas*, at p. 749:

I think that ‘securities’ means investments and ‘investments’ means, as the law now stands, investments authorised by law; that is to say, mortgages, stocks and shares, bonds, or investments authorised under the Act.

Once you say that ‘investments’ means any property at all, I do not see how you are going to exclude jewellery and wild cat investments such as gold mines in Alaska. ‘Securities’ is not confined to secured investments, but I think that it means investments and investments within the authorised range.

Having considered the facts of the present case in the light of the authorities I am not prepared to hold that the company’s stocks of bullion constituted securities for the purposes of para. 28(2)(a). The statute itself has widened the definition to include stocks and shares. I infer from that widening that the draftsman considered that without those words in parenthesis there might be some doubt as to whether stocks and shares were included. I do not believe that the legislature contemplated stocks of bullion being labelled as ‘securities’, any more than *Vaisey* J thought that it contemplated the definition including jewellery or wild cat investments such as gold mines in Alaska.

Scott J in the High Court did not address the Special Commissioner’s analysis of ‘securities’ but it remains of persuasive authority.

In *Inland Revenue Commissioners v Parker*[[14]](#footnote-14), Ungoed-Thomas J, having observed that the legislation in question, section 28 FA 1960[[15]](#footnote-15), was anti-avoidance legislation applying in a field of company operations in a commercial context, held that the legislation should be applied accordingly. ‘Securities’ is not a term of art and has no precise meaning – it might refer to security secured on real estate or by personal covenant or to shares and investments generally. After reviewing caselaw he stated:

These cases indicate, to my mind, (1) that prima facie ‘security’ is limited to security for the payment of a debt as contrasted with shares in the capital of a company; (2) that the context may extend its meaning to include shares; (3) that security by a document establishing personal liability and without charge on property is recognised as a form of security; (4) that it is questionable whether security in that sense would be within its prima facie meaning; but (5) even if it is not within the prima facie meaning of security, yet such security is a less extended meaning of that word than are shares.

Although the case reached the House of Lords the question of whether debentures were ‘securities’ was no longer a live issue.

In *Inland Revenue Commissioners v Laird Group plc*[[16]](#footnote-16) the House of Lords held that, in relation to the legislation dealing with transactions in securities, the word ‘securities’ included not only stocks and shares of every description, including preference shares, but also debentures[[17]](#footnote-17) and unsecured loan notes.

## Security and securities historically

Lord Cave thought the ‘normal’ meaning of securities was not in doubt. That was one hundred years ago, and language changes over time. The next paragraphs will look at origin and development of the word. The *Oxford English Dictionary* (OED)[[18]](#footnote-18) suggests the meaning of the word ‘security’ is in fact quite protean, though less so in the plural. It lists nine main meanings of the word grouped in two classes, the first being the state or condition of being or feeling secure, and the second the means of being or making secure, and related senses[[19]](#footnote-19). The word security derives from Late Middle English securetee and is of multiple origins; partly a borrowing from French securité (etymology Anglo-Norman and Middle French) and partly a borrowing from Latin securitas. The tax meaning is found within class (II) 5.e, chiefly in plural, originally a document held by a creditor as a guarantee of the right to payment, or attesting ownership of property, stock, bonds, etc; (hence) the financial asset represented by such a document. Also (originally and chiefly in US) such a document issued to investors to finance a business venture.

The oldest reference given in the OED, from 1425, is in meaning (I) 1.a, namely freedom from care, anxiety or apprehension; absence of worry or anxiety; confidence in one’s safety or well-being: mekenesse, soburnesse, sekurite, & reste loue wel þe cumpanye of symple pouerte.[[20]](#footnote-20) That meaning still survives in the legal and tax usage, but in its perhaps more relevant (II) 5.e meaning the earliest OED reference is from 1606, Rollock’s Lectures on the First Epistle of Paul to the Thessalonians:[[21]](#footnote-21) al the Warrands, Charters and Securities, which thou hast of thy lands.

The references given by the OED grow progressively more recognisable in modern terms:

1692   J. Locke *Some Considerations Lowering Interest* 132:  But how Securities will be mended by lowering of Interest, is, I confess, beyond my Comprehension.

1712   J. Arbuthnot *John Bull Still in Senses* viii. 33:  When I wanted Money, half a dozen of these Fellows were always waiting in my Antichamber, with their Securities ready drawn.

1746   Lord Chancellor Hardwicke in J. T. Atkyns *Rep. Cases Chancery* (1782) III. 444:  Neither South-Sea stock nor Bank stock are considered as a good security.

1848  J. S. Mill *Princ. Polit. Econ.* I. i. iv. §3 76:  He buys from the State what are called government securities; that is, obligations by the government to pay a certain annual income.

1879  *Daily News* 26 May:  Liquid Securities, or in other words, those easily convertible into cash when necessity arises.

1925   R. H. Montgomery *Financial Handbk.* vii. 526:  The financial executive ...will naturally adapt the securities offered by his company so as best to fit in with the market he is trying to reach.

1937   J. I. Bogen *Corporation Finance* xiii. 223:  Most ... successful enterprises can raise funds ...through the sale of securities.

1989   *EuroBusiness* Jan. 39/3   The British offices differ on whether convertible stocks are shares or fixed-interest securities.

2009   *N.Y. Rev. Bks.* 12 Feb. 16/1   Even commercial banks ...borrowed aggressively to invest in the mortgage-backed securities.

A slightly earlier meaning of security (II.5.d) is a person who stands surety for another, Lord Cave referred to this in his *Singer v Williams* speech as recorded above, and here some notable authors appear in the references, for example:

1600   William Shakespeare, *Henry IV, Pt. 2* i. ii. 33:  He saide sir, you should procure him better assurance then Bardolfe, he would not take his band and yours, he liked not the securitie.

1710   Jonathan Swift, *Jrnl. to Stella* 13 Nov. (1948) I. 95:  Have two people bound ... and when one dies, you fall upon the other, and make him add another security.

1786   Edmund Burke, *Articles of Charge against W. Hastings* vii. 175   Croftes offered the said Richard Johnson as one of his securities for the performance of the said contract.

1843   Charles Dickens, *Martin Chuzzlewit* (1844) xxvii. 334:  B wants a loan... B proposes self and two securities. B is accepted. Two securities give a bond.

The latter reference is particularly interesting, published as it was in the period between the reintroduction of income tax by Peel in 1842[[22]](#footnote-22) and the first Joint Stock Companies Act of 1844[[23]](#footnote-23) which is the progenitor of the Companies Acts, providing for incorporation of the ‘deed of settlement companies’ which had hitherto been used to raise funds for commercial ventures in the industrial revolution, upon registration of the deed. In the novel the villain Montague Tigg founds the *Anglo-Bengalee Disinterested Loan and Life Assurance Company*, what would now be called a Ponzi scheme in which early policyholders claims are paid off out of new policyholders’ premiums. The satire reflected the fact that life assurance companies at the time tended to reflect their supposed disinterestedness and altruistic character. So disinterested was the Anglo-Bengalee that ‘nobody can run any risk by the transaction except the office, which, in its great liberality is pretty sure to lose’.[[24]](#footnote-24)

## Securities in the company distributions and group relief legislation

Part 23 of CTA 2010 sets out the meaning of ‘distribution’ in the Corporation Tax Acts in relation to any company.[[25]](#footnote-25) Here the distinction between ‘in respect of shares’ and ‘in respect of securities’ is firmly drawn; see sections 1113 and 1114 CTA 2010. This is necessary because the aim of Part 23 is to address the indistinct border between debt and equity in the broad sense, so as to bring returns from instruments with equity characteristics into the set of instruments which give rise to ‘distributions’ in this sense, here called a company or ‘CT distribution’ and that includes returns on certain securities even though in this context they are not shares in companies.

Section 1000(1) CTA 2010 sets out the scheme determining what is a CT distribution. The comprehensive detail is not very easy to follow. It is divided into paragraphs. Paragraph A is any dividend paid by a company, including a capital dividend, which here means a dividend paid out of capital profits, not to be confused with a ‘dividend of capital nature’, which appears in the income tax charging provision for dividends from overseas companies, section 402 of the Income Tax (Trading and Other Income) Act 2005 (ITTOIA 2005). Paragraph B deals with any other distribution out of assets of the company in respect of shares, with abatements for capital repaid on the shares and any consideration received from the company for the distribution. Paragraph B has a potentially wide scope but is largely aimed at repurchases of shares. Paragraphs C and D deal with bonus issues of redeemable shares and bonus issues of securities.[[26]](#footnote-26) Paragraphs E and F deal with returns by way of interest on securities but where these returns share characteristics with equity returns: paragraph E with ‘non-commercial securities’ whose returns represent more than a reasonable commercial return for the use of the principal secured[[27]](#footnote-27) and paragraph F with returns on ‘special securities’.[[28]](#footnote-28) Paragraph G deals with transfers of assets and liabilities between a company and its members.[[29]](#footnote-29) There is a market value rule for the benefit received by a member.[[30]](#footnote-30) Paragraph H deals with a bonus issue of shares following a repayment of capital. The scheme thus aims to catch all extractions of value by members from their companies, in some circumstances even if in respect of securities (as described) rather than shares. It is not easy to apply, even so fundamental concept as what is a dividend is not at all straightforward.[[31]](#footnote-31)

In effect the legislation recognises that a firm distinction between debt securities and equity shares does not exist and proceeds to address the issue by reference to the real character of the returns.

A similar issue arises in the group relief provisions, which aim to ensure only genuine equity ownership relationships establish groups and consortia. Here the rather different approach is to define the concept of ‘equity holder’ as any person who holds ordinary shares in the company or is a loan creditor of the company in respect of a loan that is not a ‘normal commercial loan’. For this purpose, ordinary shares are all shares other than ‘restricted preference shares’.

A ‘normal commercial loan’ means a loan that satisfies all the following conditions.

First, it is a loan of, or including, new consideration (so a bonus security cannot be a normal commercial loan). It may not be convertible or carry any rights to acquire additional shares or securities.

Secondly, it does not entitle the loan creditor to any amount by way of interest which depends to any extent on the results of the company’s business or any part of it, or the value of any of the company’s assets, or which exceeds a reasonable commercial return on the new consideration lent.

Thirdly, the loan creditor is entitled on repayment to an amount which either does not exceed the new consideration lent, or is reasonably comparable to the amount generally repayable, in respect of an equal amount of new consideration, under the terms of issue of securities listed on a recognised stock exchange.

‘Restricted preference shares’ are shares which are issued for consideration which is, or includes, new consideration, are not convertible or carry any rights to acquire further shares, and do not carry any rights to dividends other than dividends which are of a fixed amount, or at a fixed rate per cent of the nominal value of the shares.

The dividends must represent no more than a reasonable commercial return on the new consideration received by the company in respect of the shares, and on repayment the shares must not carry any rights to an amount exceeding that new consideration, except in so far as those rights are reasonably comparable with those general for fixed dividend shares listed on a recognised stock exchange.

Shares that carry no rights to a dividend may be restricted preference shares for the purposes of this definition[[32]](#footnote-32) but are, however, ordinary share capital for the purposes of the general definition.[[33]](#footnote-33)

## Securities in company, regulatory and commercial law

### Company law

In United Kingdom company law, for the purpose of the prohibition of public offers by private companies, section 755(5) Companies Act 2006 (CA 2006) defines ‘securities’ as meaning shares or debentures.[[34]](#footnote-34) Shares in relation to a company are defined as meaning a share in the company’s share capital.[[35]](#footnote-35) For the purpose of evidencing and transferring title to securities without written instrument section 783 CA 2006 defines securities as meaning shares, debenture stock, loan stock, bonds, units of a collective investment scheme under FSMA 2000 and other securities of any description.

The Companies Acts define ‘equity securities’ for the purpose of pre-emption rights in relation to a company as ordinary shares in the company or rights to subscribe for, or convert securities into, ordinary shares. Ordinary shares are shares other than those that as respects capital and dividends carry a right to participate only up to a specified amount in a distribution.[[36]](#footnote-36)

### Regulatory law

The Handbook of the Financial Conduct Authority (FCA) defines ‘security’ comprehensively as any of the following investments in accordance with article 3(1) (interpretation) of the Regulated Activities Order,[[37]](#footnote-37) namely share, debenture, alternative debenture, government and public security, warrant, certificate representing certain securities, unit, stakeholder pension scheme, personal pension scheme, pension scheme which provides safeguarded benefits (in relation to advising on transfer of benefits), emission allowance and rights to most of these. There are slight variations for the listing rules and consumer credit Handbooks. The terms are defined in various articles of the RAO.

In particular, ‘shares etc’[[38]](#footnote-38) broadly means shares or stock in the share capital of any body corporate or overseas unincorporated body, but excluding shares in open-ended investment companies, building societies, co-operative and community benefit societies, industrial and provident societies and credit unions.

Article 77 of the RAO defines ‘instruments creating or acknowledging indebtedness’ as debentures, debenture stock, loan stock, bonds, certificates of deposit and any other instrument creating or acknowledging indebtedness, unless thy fall within article 78 (government and public securities). Article 77A defines alternative debenture, within the concept of alternative finance, broadly crowdfunding, online lenders, peer-to-peer lending and similar.

Thus, the regulatory definitions of security are very comprehensive and include equity interests. The United States’ Securities Act of 1933[[39]](#footnote-39) similarly uses a comprehensive definition:

The term ‘security’ means any note, stock, treasury stock, security future, security-based swap, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency, or, in general, any interest or instrument commonly known as a ‘security’, or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing.

### Commerce

In commercial practice, ‘securities’ normally includes shares. The *Oxford Dictionary of Finance and Banking*[[40]](#footnote-40) gives two meanings, which reflect the asset or assets in the issuer’s balance sheet which secures the holding, and the asset of the holder, which is a liability of the issuer:

1. An asset or assets to which a lender can have recourse if the borrower defaults on any loan repayments. In the case of loans from banks and other moneylenders the security is sometimes referred to as collateral.
2. A financial asset, including shares, government stocks, debentures, bonds, unit trusts and rights to money lent or deposited. It does not, however, include insurance policies.

According to Investopedia,[[41]](#footnote-41) ‘[t]he term security refers to a fungible, negotiable financial instrument that holds some type of monetary value. It represents an ownership position in a publicly traded corporation via stock; a creditor relationship with a governmental body or a corporation represented by owning that entity's bond; or rights to ownership as represented by an option.’ The entry goes on to assert that there are primarily three types of securities: equity, which provides ownership rights to holders; debt, essentially loans repaid with periodic payments; and hybrids, which combine aspects of debt and equity.

### Economics

In economics the difference in tax treatment between returns on shares and on securities is generally regarded as an undesirable distortion.[[42]](#footnote-42) The historically principled distinction between equity ownership shares in a company and debt securities of it is of little interest in the context of raising capital in the markets, and Ruud de Mooij has spoken of ‘the withering borderline between debt and equity instruments’.[[43]](#footnote-43) Several solutions to this distortion have been proposed and, sometimes, put into practice in various tax jurisdictions although the ‘debt/equity bias’ has proved enduring, and there has been a tendency to concentrate on the tax treatment of the company rather than considering also the tax treatment of shareholder and holders of debt securities, which is necessary to complete the picture.

In 1982 the question of debt/equity bias was examined in the United Kingdom in the Green Paper ‘Corporation Tax’[[44]](#footnote-44), written at a time when inflation was a serious problem, after the introduction of the partial imputation system in the United Kingdom in 1973 and following the report of the Meade Committee which considered the case for two different types of ‘cash flow corporate taxes’ on the ‘R’ and ‘R+F’ bases. The main difference between these is that the former takes no account of financial transactions. The R+F basis is equivalent to the ‘S’ or shareholder cash flow corporation tax basis, which looks at net cash flow to shareholders. The Green Paper noted that debt/equity bias is a feature of both ‘classical’ (company and shareholder taxed independently) and partial imputation tax credit systems, the latter leaving ‘mainstream’ corporation tax unfranked by tax on distributions.

The Green Paper went on to discuss a system which would allow deductions for distributions on shares, or at least for a market rate return on the capital just as debt interest might be deducted from interest on securities, and also a rather complicated two-rate system, at that time in use in the Federal Republic of Germany, which applied different tax rates to distributed and undistributed profits.

More recently the neutrality issue has been approached through the various concepts of ‘ACE’, allowance for corporate equity, ‘ASE’, allowance for shareholder equity, and ‘ACC’, allowance for corporate capital.[[45]](#footnote-45) The other possible approach is not to allow deductions for interest paid, see n 42 above, and as in the United States Treasury’s 1992 discussion paper of a ‘comprehensive business income tax’.[[46]](#footnote-46)

### Securities and distributed ledger technology

Blockchain is the best-known distributed ledger technology (DLT), although it is just one type of distributed ledger. This is a database that is distributed across several locations or among multiple participants, thus avoiding the need for a central authority or intermediary to process, validate or authenticate transactions. Once the parties are agreed, the files viewable by the participants are time stamped and given a cryptographical signature creating a verifiable and auditable history of all the stored information.

Blockchain is thus a particular variety of DLT arranged as a sequence of blocks and is well-known because it is the technology behind bitcoin and other cryptocurrencies. The blocks are established by ‘consensus mechanisms’, of which ‘proof of work’ and ‘proof of stake’ are the two major mechanisms used to verify new transactions, add them to the blockchain, and create new tokens.

Proof of work, pioneered by bitcoin, uses ‘mining’ to achieve those goals. Proof of work involves verification by virtual miners around the world competing to be the first to solve a mathematical puzzle. The winner updates the blockchain with the latest verified transactions and is rewarded by the network with a predetermined amount of cryptocurrency. It is energy intensive.

Proof of stake blockchains employ a network of ‘validators’ who contribute, or ‘stake’, their own cryptoassets in exchange for a chance of getting to validate new transaction, update the blockchain, and earn a reward. The network selects a winner based on the amount of cryptoassets each validator has in the pool and the length of time they have held it. Once the winner has validated the latest block of transactions, other validators can attest that the block is accurate. It is less energy intensive and more scalable than proof of work.

This explanation is intended to demonstrate that the technology is apt to get in the way of the fact that distributed ledger is just a recording mechanism, a modern secure way of achieving the same result as a share certificate or bond security document does in relation to equity interests and debt. The term ‘non-fungible token’, or NFT, is applied to a financial security stored in a blockchain, and also to other content that can be digitised such as artworks and music. The law in this area is still developing[[47]](#footnote-47) and there are arguments that the token is separate from an underlying asset, more like a depository receipt.

The technology can be applied to a variety of different uses. The FCA defines two classes of regulated tokens, ‘security tokens’ and ‘e-money tokens’. Any others are un-regulated and this includes ‘utility tokens’, which can be redeemed for access to a specific product or service that is typically provided using a DLT platform, artworks being one example. Cryptocurrencies (or ‘payment tokens’ or ‘exchange tokens’) also fall into the unregulated category unless they are designed to maintain a stable relationship to one currency and are thus e-money tokens.

Cryptocurrency proponents view cryptocurrencies as money, as they rather imperfectly reflect the three characteristics generally attributed to currencies and money, store of value, means of exchange and unit of account. They are imperfect because of their volatility and some critics view them as little better than a Ponzi scheme, suggested by one authority to be ‘speculative assets that can cause major damage to society’.[[48]](#footnote-48)

There is considerable tension between the crypto firms, some of whom declare aspiration to a libertarian Utopia where blockchains remove the need for financial intermediaries and regulators, and the regulators themselves who see dangers from money laundering, to tax systems, and to financial regulation, including investor protection, systemic risk and fair market competition. Intensive lobbying has resulted.[[49]](#footnote-49) At the time of writing, the OECD (Organization for Economic Cooperation and Development) is developing a CryptoassetsReporting Framework (the ‘CARF’), designed to ensure the collection and exchange of information on transactions in cryptoassets.[[50]](#footnote-50)

Regulators have been considering whether and which cryptoassets count as securities, which carry strong disclosures by issuers, as commodities, which are regulated more lightly focusing on the prevention market manipulation, or as cryptocurrencies. So-called stablecoins are a particular issue. These are supposed to track something stable, generally the dollar or another hard currency, but in May 2022 a stablecoin called terraUSD lost value in spite of its dollar tracking after luna, an affiliated token which terra algorithmically tracked[[51]](#footnote-51), collapsed in value. Moreover, the largest stablecoin called tether temporarily failed to maintain parity and ‘broke the buck’, falling to 95.11 cents on the dollar, although it apparently continued to redeem at par when called.[[52]](#footnote-52)

One authority, formerly chair of the Federal Deposit Insurance Corporation of the United States, has called for regulation if stablecoins, one possibility being for the Securities and Exchange Commission, although this would require the SEC to view stablecoins as securities, which would arguably be inconsistent with the traditional view that a security includes an investor expectation of profit, since most stablecoins do not yield returns.[[53]](#footnote-53) The problem appears to be the opacity of the accounting for ‘conventional’ stablecoins, they do not wish to reveal their ‘secret sauce’, and in some cases the functioning of the algorithm designed to maintain the necessary value automatically. While the financial markets generally also suffered reverses following rises in interest rates, which affected the riskier asset classes generally, the problem appears to be more acute among cryptocurrency stablecoins for the very reason that they are not securities and are not fiat currencies backed by governments either. Some suggest there are problems with cryptosphere ‘plumbing’.[[54]](#footnote-54)

Whatever view one takes in that debate, there seems on the face of it little doubt that, depending on their precise terms, security tokens will be securities for regulatory and tax purposes.[[55]](#footnote-55) This will include related derivatives, those that take their value by reference to security tokens. HMRC publishes a Cryptoassets Manual, which reflects the classification of cryptoassets into exchange tokens, utility tokens, security tokens and stablecoins.[[56]](#footnote-56)

The manual emphasises that it is the nature of the cryptoassets and how they are used rather than any definition or description of them that is the starting point. Most UK resident investors will be liable to chargeable gains on disposal rather than to income taxes, though there are exceptions where the taxpayer is actively ‘mining’ or ‘staking’, is otherwise undertaking a trade, or is being remunerated for services undertaken. Chargeable gains accrue on disposals of the assets.

There is no international consensus at present on the treatment of cryptocurrencies and cryptoassets generally. The legal status of security tokens and their offering differs greatly. Some states, like El Salvador, have embraced cryptocurrency with enthusiasm, it was the first country to adopt bitcoin as official currency. Others, notably China and India have threatened or implemented bans. In general, policies are under development. In the European Union, MiFID II[[57]](#footnote-57) covers most securities and security tokens, but a special regulatory framework the MiCA Regulation[[58]](#footnote-58) is being developed. The United States applies its existing securities laws[[59]](#footnote-59). Australia distinguishes between financial and non-financial tokenised securities. The United Kingdom distinguishes the three categories, security, exchange and utility tokens as mentioned above.[[60]](#footnote-60) Switzerland regulates security tokens under a series of laws defined by FINMA, the Swiss Financial Market Supervisory Authority. Japan has developed a framework for regulating security tokens and their offerings. South Korea has banned sales of security tokens and their offerings, but that policy is under review. Canada proceeds on a case-by-case basis. The general policy is more favourable to security tokens and their offering than to coins, for the reasons discussed above.

## Conclusion

Even recognising that Lord Cave’s statement was drafted more than a hundred years ago the subsequent case law suggests that the normal meaning of securities was open to quite a lot of doubt and has a number of meanings in different fields. Securities or a security may refer to an extension of the simple promise or obligation to repay an advance, or it may mean an instrument which supports the terms of the contract between obligor and obligee. It may include a bill of exchange, guarantee or promissory note. It may also mean the real security or collateral, the right over property by which the enforcement of a liability is facilitated.

Securities is certainly a chameleon word that takes its colour according to context and has different scope and meanings according to its tax, regulatory or commercial usage. It is of early origin and its meaning has developed, but not in a way fundamentally different from that origin. Its meaning is relevant, and a matter of some dispute, in relation to the very newest technologies.

1. \*Senior policy and technical adviser, Her Majesty’s Revenue and Customs. The views expressed are not necessarily those of the Commissioners for Revenue and Customs.

 [1920] UKHL 386; 7 TC 419 at 431. Not to be confused with *Williams v Singer* [1920] UKHL 2, which concerned the assessability of trustees and beneficiaries. See ‘Seven appeals and an acquittal: the Singer family and their tax cases’, David Parrott and John F Avery Jones, BTR 2008, 1, 56-94. [↑](#footnote-ref-1)
2. Sewing machine. [↑](#footnote-ref-2)
3. Cases IV and V of Schedule D ended their life within section 18(3) Income and Corporation Taxes Act 1988, before being rewritten under the Tax Law Rewrite project. [↑](#footnote-ref-3)
4. The author recollects sharing a room in Somerset House, then Inland Revenue headquarters, around 1990 with an officer who had the responsibility of certifying whether instruments were securities for a certain purpose. Asked whether securities included shares, he said ‘that’s a very interesting question’. Which he did not answer. [↑](#footnote-ref-4)
5. Ch 1 pt 13 Income Tax Act 2007. [↑](#footnote-ref-5)
6. Along with many trainee tax inspectors in the days before Tax Law Rewrite. [↑](#footnote-ref-6)
7. His Lordship might have said 1803, since Peel’s 1842 act (5 & 6 Vict c 35) was largely a re-enactment of Addington’s Schedules and Cases set out originally in an act of 1803 (43 Geo 3 c 122) subject to fairly minor developments when the income tax code was repealed in 1816 following the end of the Napoleonic wars. See following text. [↑](#footnote-ref-7)
8. 46 Geo III c 65. [↑](#footnote-ref-8)
9. [1895] 2 QB 589. [↑](#footnote-ref-9)
10. (1971) 47TC300. [↑](#footnote-ref-10)
11. The famous ‘Ramsay principle’ case (1981) 54TC101. [↑](#footnote-ref-11)
12. There is a parallel here with shares in companies, which include any interest of a member in a company for the purposes of company distributions (section 1117(1) CTA 2010) but the issue of a share certificate is not essential, subject to Companies Act provisions for Companies Act companies or other relevant company law. See the discussion at CTM00513 in HM Revenue and Customs’ (HMRC) Company Taxation Manual. [↑](#footnote-ref-12)
13. (1990) 63TC41. [↑](#footnote-ref-13)
14. (1966) 43TC396. [↑](#footnote-ref-14)
15. Now reflected in the transactions in securities legislation referred to in ‘Tax definitions’ above. [↑](#footnote-ref-15)
16. [2003] BTC385. [↑](#footnote-ref-16)
17. Debenture is one of the limited set of words which are generally used to mean significantly different things on opposite sides of the Atlantic. Usage in the United States generally connotes a bond which is unsecured, while in British usage it is generally one secured by company assets. [↑](#footnote-ref-17)
18. OED Third Edition, September 2011, published online March 2022. [↑](#footnote-ref-18)
19. This is reflected in the securities issued by a company, a liability in its balance sheet, and the correlative security held against them, an asset. [↑](#footnote-ref-19)
20. Meekness, soberness, security and rest love well the company of simple poverty. The *Oxford Middle English Dictionary* suggests this usage of loue is erroneous. ‘þe’ means ‘the’ as it contains the Anglo-Saxon symbol or letter ‘thorn’,þ, which makes a ‘th’ sound, giving rise to the error ‘ye olde’ pronounced with a ‘y’ beloved of licensed establishments. [↑](#footnote-ref-20)
21. W. Arthur and H. Charteris, Rollock’s Lect. *1st and 2nd Epist. Paul to Thessalonians* (1 Thess.) xvi 200. Robert Rollock lived in the second half of the 16th Century and was the first regent and first principal of the University of Edinburgh. The fuller quote is ‘It is not permitted to a King, to eate bread except he labour for it: (and surelie his labour is an heauie labour) No, for al the Warrands, Charters and Securities, which thou hast of thy lands, be thou Earle, or Lord, or Barron, except thou eate the labour of thy owne hands, thou eatest not lawfullie, but, thy eating is accursed’. [↑](#footnote-ref-21)
22. See n 7 above. [↑](#footnote-ref-22)
23. 7&8 Vict c 111. [↑](#footnote-ref-23)
24. Liz Mcfall (2007) ‘The Disinterested Self’, *Cultural Studies*, 21:4-5, 591-609. [↑](#footnote-ref-24)
25. Company is defined at s 1121 CTA 2010 in substance as meaning any body corporate or unincorporated association but does not include a partnership. [↑](#footnote-ref-25)
26. The aim here is to address distributions of value without any assets leaving the company, and in the days of payable tax credits given to recipients the distributions were ‘non-qualifying’ so they could not give rise to credits in these circumstances. [↑](#footnote-ref-26)
27. S 1005 CTA 2010. [↑](#footnote-ref-27)
28. These are defined at ss 1015 to 1018 CTA 2010 broadly in terms of equity-like characteristics – convertible securities, business results-dependent returns, securities connected with shares, ‘equity notes’ as defined. Returns on bonus shares are included in the definition. [↑](#footnote-ref-28)
29. Both the drafting papers of FA 1965 (TNA IR40/16687), where the company distributions scheme originated, and the ‘Notes on Clauses’ suggest that what is now paragraph G of s 1000(1) CTA 2010 was intended as a sweep-up provision, although the Special Commissioners somewhat tentatively disagreed with this interpretation in *Noved Investment Co v HMRC* [2006] UKSPC 521. [↑](#footnote-ref-29)
30. In s 1020(3) CTA 2010. [↑](#footnote-ref-30)
31. See the judgment of Judge Rachel Short in *Alexander Beard v HMRC* [2022] UKFTT 00129 (TC). This case concerned a distribution under the Companies (Jersey) Law. [↑](#footnote-ref-31)
32. S 160 CTA 2010. [↑](#footnote-ref-32)
33. S 1119 CTA 2010. See *HMRC v McQuillan* [2017] UKUT 0344 (TCC). [↑](#footnote-ref-33)
34. A debenture is defined in the Companies Acts as including debenture stock, bonds and any other securities of a company, whether or not constituting a charge on the assets of the company: s 738 CA 2006. [↑](#footnote-ref-34)
35. S 540 CA 2006. S 1161(2) goes on to define shares where a company has capital but no share capital (as shares in the capital) and in relation to an undertaking without capital (as interests conferring any right to share in profits or liability to contribute to losses of the undertaking, or creating an obligation to contribute to debts or expenses in a winding up). [↑](#footnote-ref-35)
36. S 560(1) CA 2006. [↑](#footnote-ref-36)
37. The Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 SI 2001 No.544. Known as the RAO. [↑](#footnote-ref-37)
38. Defined at art 76 of the RAO. [↑](#footnote-ref-38)
39. At S 2. [↑](#footnote-ref-39)
40. Third Edition (2005). [↑](#footnote-ref-40)
41. Entry written by Will Kenton, updated 20 March 2021. [↑](#footnote-ref-41)
42. An important one according to some economists. Stian Westlake and Jonathan Haskel in ‘An Agenda for the Intangible Economy’ (December 2001), *City Journal*, Manhattan Institute for Policy Research, suggest that intangible assets are of increasing importance in national economies, and the consequential comparative absence of tangible assets in balance sheets able to support tax-favoured debt finance is a significant brake on efficient development of the market economy. The authors (one of whom is an external member of the Bank of England Monetary Policy Committee) favour ending the tax advantages of debt finance, thereby levelling the playing-field between tangible and intangible investment and, they believe, helping to relieve inequalities and economic stagnation by lifting ‘the curse of collateral’. These ideas are developed in ‘Capitalism without Capital, The Rise of the Intangible Economy’ (Princeton, Princeton University Press, November 2017) and ‘Restarting the Future’ (Princeton, Princeton University Press, March 2022). [↑](#footnote-ref-42)
43. ‘Tax biases to debt finance: assessing the problem, financing solutions’, *IMF Staff Discussion Note 11/11*. Ruud de Mooij is an adviser in the International Monetary Fund’s Fiscal Affairs Department. [↑](#footnote-ref-43)
44. Cmnd 8456. [↑](#footnote-ref-44)
45. There is an interesting discussion, which combines the concept of these allowances with a destination base, in Shafik Hebous and Alexander Klemm, ‘A destination-based allowance for corporate equity (November 2018) *IMF Working Paper* WP/18/239. See also Chapter 17 of ‘Taxing corporate income’ in Mirrlees et al ‘Tax by Design’ (Oxford, Oxford University Press, September 2011). [↑](#footnote-ref-45)
46. ‘A Recommendation for Integration of the Individual and Corporate Tax Systems’ (Department of the Treasury, December 1992). [↑](#footnote-ref-46)
47. See, for example, *Osbourne v Parsons Unknown* [2022] EWHC 1021 (Comm). [↑](#footnote-ref-47)
48. ‘ECB official likens cryptos to Ponzi scheme in call for tighter regulation’, *FT Weekend*, 30 April/1 May 2022. The official in question was Fabio Panetta, executive member of the European Central Bank with oversight of the Bank’s work on the digital Euro. [↑](#footnote-ref-48)
49. See ‘Crypto’s crew’, *The Economist*, 11 December 2021, 76. [↑](#footnote-ref-49)
50. ‘Cryptoasset reporting framework and amendments to the common reporting standard’, Public Consultation Document, 22 March ­– 29 April 2022, OECD. [↑](#footnote-ref-50)
51. Meaning using historical information and ‘deep learning’, a form of artificial intelligence, to predict movements. [↑](#footnote-ref-51)
52. It is worth recalling that, after the collapse of Lehman Brothers on 16 September during the 2008 financial crisis, even greater panic set in two days later when Primary Reserve Fund, a money market mutual fund broke the buck due to the loss of value of its Lehman fund holdings. [↑](#footnote-ref-52)
53. See ‘Regulate Stablecoins please!’, *The Economist*, 10 June 2022. The author is Sheila Blair, who observes that the United States has a plethora of regulatory agencies, none of whom seem to be entirely suitable for the task. [↑](#footnote-ref-53)
54. See ‘The crypto infrastructure cracks’, *The Economist*, 12 May 2022. [↑](#footnote-ref-54)
55. One simple definition of security token is ‘essentially a digital form of traditional securities’: coinmarketccap.com. [↑](#footnote-ref-55)
56. See HMRC Cryptoassets Manual CRYPTO10100. [↑](#footnote-ref-56)
57. Markets in Financial Instruments Directive 2014/65/EU (*OJ* L 173, 12 June 2014). Art 4(1) (44) defines transferrable securities. [↑](#footnote-ref-57)
58. Markets in Cryptoassets Regulation. [↑](#footnote-ref-58)
59. The so-called Howey test, based on a Supreme Court judgment, for whether an investment qualifies as an ‘investment contract’ and so would be considered a security is arguably outdated in relation to cryptoassets. [↑](#footnote-ref-59)
60. The Economic Secretary to the Treasury, John Glen MP, delivered a speech to the Innovate Finance Global Summit on 4 April 2022 which set out the aim for the United Kingdom to become a ‘global hub’ for cryptoassets with new regulations for stablecoins and proposals for the Royal Mint to issue NFTs as collectibles. The possibility of using DLT to issue government debt was to be explored, and the application of tax laws reviewed. [↑](#footnote-ref-60)