

# The courts seeking to determine the spirit of the law

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### [KPMG report:](#)

*The Court of Appeal judgment in Prudential plc v HMRC<sup>1</sup> was published on 25 June 2009. The Court of Appeal found in favour of HMRC, following the decisions of the Special Commissioners and the High Court.*

*The case revolves around hedging transactions involving off-market swaps. In 2002 Prudential entered into currency swap arrangements with the Royal Bank of Scotland and Goldman Sachs International. The swaps operated as hedges of two foreign exchange exposures in Prudential. Prudential made upfront payments of £65m and £40m and were seeking a tax deduction for the total of £105m paid up front in the accounting periods in which the payments were made. The legislation in question (foreign exchange rules in Finance Act 1994) has now been repealed but the Special Commissioners decision was of interest because of its analysis of the unallowable purpose test. However there has been no further discussion on this point in either the High Court or Court of Appeal decisions.*

*This case is, however, a reminder that the interpretation of a single phrase cannot be done in isolation without regard to the logic of the relevant area of legislation even in cases where the tax legislation is highly prescriptive.*

I have added the emphasis. The reason is obvious: this is further evidence that the courts are seeking to determine the spirit of the law.

It's rather pleasing that in the process they kick a scheme by some 'usual suspects' into touch. I believe it was concocted by Ernst & Young — another in that category, and no doubt why KPMG reported it as they did!