TC03969

Appeal numbers: SC/3083-87/2009

INCOME TAX – in specie contribution to funded unapproved retirement benefits scheme – whether paid in respect of particular directors or employees – basis of allocation to employees in absence of allocation by contributing company – whether arrangements a sham or other pretence

FIRST-TIER TRIBUNAL
TAX CHAMBER

(1) MR NORMAN SAMUEL PHILPOTT	**First Appellant**
(2) MR DAVID WILLIAM SCOTT LAW	**Second Appellant**
(3) The Personal Representatives of MR DANIEL JOSEPH McKILLOP	**Third Appellant**
(4) MR JOHN BRIAN LAW	**Fourth Appellant**
(5) The Personal Representatives of MR VICTOR ALBERT LAW	**Fifth Appellant**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS	**Respondents**

TRIBUNAL: JUDGE MALCOLM GAMMIE CBE QC
MRS GILL HUNTER

Sitting in public at Bedford Square, London WC1 on 3, 4 and 10 June 2013

Christopher Sokol QC instructed by Alan Pink Tax for the Appellant

James Rivett, counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs for the Respondents

DECISION

Introduction

1. These are appeals by Mr N S Philpott and four other individuals against closure notices dated 19 August 2008 in respect of their tax returns for the year ended 5 April 2006. The officer's conclusion in each case was that their self-assessments omitted the benefit of an *in specie* contribution to a funded unapproved retirement benefits scheme (the "**WJL FURBS**", also referred to as "**the Scheme**") made by W J Law Group Ltd ("**the Company**").

2. The four other individuals in respect of whose self-assessment returns for the same tax year the inspector issued closure notices were Mr D W S Law, Mr D J McKillop, Mr J B Law and Mr V A Law. Each of them was either a director of the Company or of a subsidiary of the Company. They each appealed the closure notice in their case and the five individuals' appeals were consolidated and heard together. Subsequent to the year in question Mr V A Law and Mr D J McKillop died and their appeals have been pursued by their executors. The amount involved for each of the five individuals was as follows:

Taxpayer	Increase in taxable income	Additional tax sought
Mr N S Philpott	£3,309,666	£1,323,866.40
Mr D W S Law	£3,309,666	£1,323,554.80
Mr D J McKillop	£248,000	£99,200
Mr J B Law	£3,309,666	£1,323,866.40
Mr V A Law	£148,000	£59,200

3. We refer to the five individuals collectively as "**the Appellants**". Given that three Appellants are "Mr Law", we shall refer to each of them individually by their initials: NSP, DWSL, DJM, JBL and VAL.

4. In addition to the documents produced to us, each of NSP, DWSL and JBL gave evidence and was cross-examined by Mr Rivett for the Commissioners. We also received evidence from Mr Anthony Glover, whose firm McCreery Turkington Stockman acted as accountants and auditors to the Company, to W J Law & Co LLP and to the WJL FURBS, and from Mr Colin McDowell, the chartered surveyor with DTZ McCombe Pierce LLP ("**DTZ**") who performed a professional valuation of the properties that formed the *in specie* contribution to the WJL FURBS. Finally, we heard the evidence of Mr Richard Green, a director of Avenue Corporate Planning Ltd ("**ACP**"), a professional trustee company.

The issue for our determination

5. The basic transactions involved in the arrangement with which we are concerned were relatively straightforward—

(1) On 27 February 2006 the Company established the WJL FURBS;

(2) On 16 March 2006 the Company made cash contributions totalling £34,000 to the WJL FURBS allocated to each of the Appellants;

(3) On 31 March 2006 the Company transferred three parcels of development land in Northern Ireland ("**the Properties**") to the WJL FURBS;

(4) On 1 April 2006, DWSL, JBL, NSP, the Company and the WJL FURBS agreed to carry on business as members of W J Law & Co LLP ("**WJL LLP**");

(5) On 1 April 2006 the Trustees of the WJL FURBS declared themselves trustee of the Properties for WJL LLP;

(6) On 25 September 2006 the WJL FURBS awarded VAL a tax free cash payment of £150,000 and JBL a like payment of £3,000,000;

(7) On 12 October 2006 the WJL FURBS awarded DJM a tax free cash payment of £250,000.

6. The Properties were initially valued by DTZ at £10,325,000 as at 31 March 2006 but this was later reduced to £7,270,000. Mr McDowell of DTZ performed the latter valuation of the Properties on 27 November 2008 and gave evidence to the effect that the valuation represented a fair open market value of the Properties at 31 March 2006. Otherwise we received no valuation evidence and we are not required to reach any view on that issue. The Properties had a cost to the Company (as per its accounts) of £3,236,577.

7. The sole issue with which we are concerned is the liability of the Appellants in respect of the in specie contribution of the Properties to the WJL FURBS. No issue arises in respect of the payments referred to in paragraph 5(2) above, which were taxed as sums paid in respect of each of the Appellants under section 386 Income Tax (Earnings and Pensions) Act 2003 ("**ITEPA**"). The Appellants conceded (having regard to the Court of Appeal's decision in *Irving v Revenue and Customs Commissioners* [2008] STC 597) that the Company's contribution of the Properties to the WJL FURBS, although *in specie*, was also a "sum paid" within the meaning of section 386. The contribution of the Properties could therefore count as employment income under that section. The Appellants contended, however, that none of the Appellants was taxable under that section in respect of any part of the value of the Properties for the year ended 5 April 2006 because the Company did not contribute the Properties in respect of any particular individual who might benefit under the WJL FURBS and neither the Company nor the Trustees of the WJL FURBS had sought to allocate any part of the value of the Properties to any of the Appellants.

8. HMRC put the Appellants to proof of the arrangements into which they had entered. HMRC contended that a proportionate part of the value of the Properties had in fact been expressly and/or impliedly paid in respect of each Appellant. In the

alternative, HMRC contended that a proportionate part of that value had in fact been expressly and/or impliedly allocated to each Appellant. In the further alternative, HMRC contended that if there had been no express or implied allocation, the value should be apportioned between the Appellants equally in accordance with section 388 ITEPA. In the further alternative HMRC contended that the Appellants' arrangements amounted to a sham or other pretence. Finally, HMRC said that the Appellants had failed to discharge the burden of proof that they had to satisfy to displace the amendments made by the closure notices and that we should therefore confirm the officer's amendments as made.

9. As this suggests, our findings of fact are crucial to the outcome of the Appellants' appeals. We are also called upon to consider carefully the terms of the WJL FURBS, to decide whether, as part of the Appellants' arrangements, the Properties were in fact properly vested in the Trustees on the terms of the WJL FURBS or on some other terms and, if on the terms of the WJL FURBS, what precisely those terms envisaged. It is by reference to our findings of fact and our view of the terms of the WJL FURBS that we must determine how ITEPA operates to charge the Appellants to tax (if at all) and whether the officer's closure notices and amendments can stand.

10. Finally, by way of introduction, we will mention the fact that on 1 April 2006, 19 December 2006 and 7 April 2008, JBL made substantial gifts from his capital account with the WJL LLP to NSP and DWSL on terms that each of them immediately introduced the gifted amounts into their capital accounts with the WJL LLP. As will appear, the relationship (if any) of these gifts to the arrangements as a whole was largely unexplained (see paragraph 30 below).

The Facts

The establishment of the FURBS

11. The Company is a long established house builder and property developer, operating primarily in Northern Ireland. Its directors at the time comprised JBL, DWSL, VAL and NSP. W J Law Ltd was a subsidiary of the Company. Its directors were JBL, DJM, DWSL and NSP. JBL had 30 years' experience as a builder; he had the largest shareholding in the Company and we conclude that he was the dominant influence in the Company. In 2006 he was in the process of handing over the business to his son, DWSL.

12. The Company was run on an 'informal' family basis in the sense that the directors might well take decisions without the formality of a board meeting and without the decision necessarily being recorded in board minutes. NSP and JBL explained, however, that there were meetings every Friday at which operational business matters would be discussed. Financial matters were not usually covered at these meetings. No minutes of any board meeting of the Company were produced to us other than the Board Resolution establishing the WJL FURBS.

13. On 23 February 2006, the Company resolved to set up a FURBS and to make an *in specie* asset contribution to it, "*for the purposes of ensuring that company employees were adequately remunerated, and that future retirement benefits for scheme members, both current and future, were provided for*". The Board Resolution

does not refer to the cash contributions that were subsequently made to the WJL FURBS.

14. On the same day NSP signed forms on behalf of the Company requesting ACP to provide the documentation to establish the WJL FURBS and provide the members with details of the benefits of their membership. There was no evidence that any member was ever provided with those details and we therefore find that no details were in fact provided (although, as we shall subsequently record, we find that the intended benefits to be derived by JBL, VAL and DJM were known and agreed in advance). On the same day NSP and DWSL signed membership application forms containing their member details. These forms were sent by BJM (the 'name' of a firm of chartered accountants and not the initials of any individual engaged in these arrangements) to ACP on 24 February 2006.

15. Following the Company's resolution of 23 February 2006, a Trust Deed establishing the WJL FURBS was entered into on 27 February 2006 between the Company, ACP and the Appellants. ACP and the Appellants were appointed the first Trustees and ACP was appointed the first Scheme Administrator. The Deed recited that the WJL FURBS was established to provide retirement and other benefits in respect of the service of such persons as became members. To avoid any confusion with the members of the WJL LLP, we refer to members of the WJL FURBS as "scheme members".

16. On 10 March 2006 QED Tax Consulting ("**QED**") sent ACP membership application forms (dated 9 March 2006) and member details in respect of JBL, VAL and DJM. NSP suggested in evidence that one reason for the delay in introducing these three further members was that DJM wanted to speak to his wife about the arrangement before committing to it but he denied that this was because they wanted to discuss what DJM was to get from the arrangement.

17. There was a later letter, dated 6 April 2006, in which NSP wrote to ACP to inform ACP that the Appellants had been invited to apply for membership in addition to holding the position of Trustees. ACP was requested to accept the five individuals into membership, "*as no application forms are, to my knowledge, in existence at this time*". In cross-examination NSP was unable to say why he had written this letter given the submission to ACP in February and March of membership application forms for the Appellants.

18. We find that the original application forms were signed and submitted as appears from the documents. We assume that NSP wrote in error, possibly because the earlier forms had been submitted by BJM and QED. We do not conclude that NSP's letter indicates that the Appellants were not members (or were not in process of being accepted as members) of the WJL FURBS at the time at which the Company made its cash and *in specie* contributions.

19. A Trustees' minute of 14 April 2006 signed by NSP and DJM records a telephone conversation with Mr Green of ACP and confirms that all five individuals had been admitted as members of the WJL FURBS. The Trustees' minute is addressed "Dear All" and was evidently sent to each of the Appellants and to ACP. The minute does not state when the Appellants were admitted as members. We find that the Appellants

became scheme members pursuant to the applications submitted on 24 February and 10 March 2006. We conclude (having regard to the cash contributions made on their behalf on 16 March 2006) that they were all admitted members of the WJL FURBS prior to the Company's *in specie* contribution of the Properties.

20. At the time the Company had 21 employees, 12 of whom were said in correspondence to have become or were eligible to become members of the WJL FURBS. The Appellants were the only individuals "to have become" scheme members and although the names of an additional 7 individuals who "were eligible" for membership were supplied to HMRC in correspondence none of them was ever actually admitted to scheme membership.

21. The Trust Deed and the Rules appended to it required that scheme members were given written particulars of the essential features of the FURBS. We saw no evidence that this was done for the Appellants and we find that it was not. It was certainly never done for anyone else. NSP could not recall anything about this aspect of the WJL FURBS. The reason why no other individual was admitted a scheme member was stated in correspondence and by NSP in evidence to be the collapse of the Company's business not long after the WJL FURBS was established.

22. By a letter dated 16 March 2006 (see paragraph 61 below), the Company paid £34,000 to the WJL FURBS, allocated as follows: NSP, DWSL and JBL £10,000 each and DJM and VAL £2,000 each. The Appellants included these contributions in their self-assessment returns for the year ended 5 April 2006. No issue arises in respect of the liability to tax of these contributions although, as we shall record, they may be relevant to the allocation of the *in specie* contribution of the Properties.

23. On 31 March 2006, the Company transferred the Properties to the Trustees of the WJL FURBS (the Appellants and ACP). A valuation dated 30 March 2006 by DTZ, a firm of independent chartered surveyors, valued the Properties at the time at £10,325,000. A later valuation dated 27 November 2008 by DTZ valued them as at 31 March 2006 at £7,270,000. NSP said in evidence that based on his experience of the local property market he thought the initial valuation was too high. The Company initially claimed a deduction for corporation tax purposes for the higher amount but this was later adjusted to the lower amount. We are not concerned with the Company's tax deduction and do not know whether it is finally agreed or is still under enquiry. Apart from the Board Resolution and the land transfers, no other documents or correspondence was produced (and no correspondence was said to exist between the Company and the Trustees) regarding the Company's contribution of the Properties to the WJL FURBS.

24. On 1 April 2006 DWSL, JBL, NSP, the Company and the WJL FURBS ("**the Members**") entered into an agreement under which the Members agreed to carry on business together as a limited liability partnership known as the W J Law & Co LLP. On the same date the Trustees signed a declaration to the effect that they held the Properties as trustee for sale for the WJL LLP. The WJL LLP was incorporated under the Limited Liability Partnership Act (Northern Ireland) 2002 on 24 April 2006.

The WJL LLP

25. The WJL LLP was established to carry on "the Business", which is unhelpfully defined as "the profession trade or business". The WJL LLP accounts for the period ended 30 April 2007 describe its business as "property development".

26. Clause 8 of the LLP Agreement states that "*each of the Members shall acquire as at the Commencement Date a Member's Share equal to the amount or value of any Contribution made by him on the Commencement Date*". The definition of "Commencement Date" fails to specify any date but we find that the Commencement Date was intended by all concerned to be the date on which the LLP Agreement was signed, i.e. 1 April 2006. Any Member making any contribution after the Commencement Date is to acquire a new share or augment his existing share by the amount or value of the contribution.

27. The initial contributions made by each of the Members (as reported in correspondence) were evidently as follows:

JBL	£10,608,737
DWSL	18,012,811
NSP	5,017,650
The Company	8,680,173
WJL FURBS	10,325,000
Total	52,644,371

We assume (although it is not stated in the correspondence) that these figures include the value of JBL's gifts to NSP and DWSL on 1 April 2006 (see paragraph 29 below).

28. The income profits and losses were to be distributed "*as the partners from time to time*" decided. Capital profits and losses were to be held as follows: JBL 11.2%; DWSL 66%; NSP 22.8%; the Company 0% and WJL FURBS 0%.

29. On 1 April 2006 JBL and NSP executed a deed of assignment. This recites that on that date JBL has transferred £5,000,000 to NSP from his capital account in WJL LLP. It also recites that NSP has agreed to introduce the £5,000,000 into NSP's capital account in WJL LLP. Under a second deed of assignment of the same date between JBL and DWSL, JBL transferred £2,500,000 to DWSL from his capital account in WJL LLP and DWSL agreed to introduce £2,500,000 into DWSL's capital account in WJL LLP. JBL and DWSL executed two further deeds of assignment to similar effect on 19 December 2006 (in relation to £1,000,000) and on 7 April 2008 (in relation to £3,000,000).

30. Mr Rivett cross-examined JBL about these arrangements but it is fair to say that JBL was unable to recall anything useful about them. He also cross-examined NSP about his position as a Member of the WJL LLP. This did not add a great deal of clarity to the matter but the suggestion was, in effect, that NSP was content to receive nothing from the WJL FURBS because the benefit he was obtaining from the overall arrangement was a contribution to his capital account in the WJL LLP, a share in the profits and a 22.8 per cent interest in capital profits. NSP acknowledged that his capital account on becoming a Member of the WJL LLP could be viewed as in effect

equivalent to a further pension scheme contribution for his benefit. He appeared to accept that his share in the WJL LLP was his 'reward' and as a result he was content to be getting nothing from the WJL FURBS. DWSL was not asked about these arrangements but we assume that a similar suggestion could be made, although we do not know how DWSL would have responded to the suggestion.

31. The first accounts for WJL LLP shows as "Equity – Members' other interests – members' capital" the sum of £35,877,546 (being the balance remaining after repayments). The Contributions by members are shown as £53,405,547 (a slight discrepancy from the figures shown in paragraph 27 above) and payments to members are shown as £22,892,591, of which £17,528,001 were repayments of capital (the balance of £5,364,590 being the profit available for distribution to members). The accounts confirm that the Company introduced capital of £8,680,173 and the WJL FURBS capital of £10,325,000 through its contribution of the Properties. The capital contributions by other members are not stated in the accounts. There is an increase in bank loans of £16,686,185.

32. The later accounts of the WJL LLP for the year ended 31 March 2009 show a prior year adjustment reducing the WJL FURBS' contribution to £7,270,000. Because parts of the Properties were sold in the years to 31 March 2007 and 2008, an adjustment was also made to the profit shares of the Company and the WJL FURBS. Bank loans by that period had increased to £37,897,139 secured over the LLP's assets and the WJL LLP was joined in cross guarantees with the Company, W J Law Ltd and the WJL FURBS.

The WJL FURBS Trust Deed and Scheme Rules

33. The Trust Deed is dated 27 February 2006 and is made between the Company and the Appellants and ACP as Trustees. Recital 2 states that the Company has decided to establish a Retirement Benefits Scheme "*for the sole purpose of providing retirement and other benefits in respect of the Service of such persons as become members*" and Clause 1 of the Deed establishes the Scheme "*under the Trust the full terms and conditions of which are contained in the Deed*". Recital 3 states that the Company "*has given written particulars of the essential features of the Scheme to each individual member who will be invited to become a Member at the Commencement Date*" (i.e. 27 February 2006). We have concluded that this was never done.

34. Clause 2 appoints the Trustees as the first Trustees of the Scheme and Clause 3 appoints ACP as the first Scheme Administrator. That appointment is expressed to be "*subject to any terms and conditions which are agreed in writing*" between the Company and ACP. There was no evidence that the Company and ACP agreed any terms and conditions other than those appearing in the Trust Deed and the Scheme Rules.

35. Clause 5 requires the Company to collect any contributions required to be made by scheme members and account to the Trustees for those contributions. There was no evidence to suggest that it was ever contemplated that scheme members should make any contributions to the WJL FURBS. Clause 5 also provides that contributions may be paid "*by the Employers of the employees concerned under the provisions of the Rules*", the "employees concerned" being "*their respective employees as are*

Members". Clause 5 also requires the Company to keep "*a record of the contributions that have been made on behalf of each Member.*"

36. Clause 6(i) contains a wide investment power entitling the Trustees in their absolute discretion to deal with any monies or assets not required to meet current liabilities in respect of benefits as if they were entitled to the monies or assets beneficially. Clause 6(iii) contemplates that the Trustees shall invest all or part of a "Members (*sic*) interest" in accordance with written directions received from that scheme member. The Trustees are not liable for the investment performance of assets invested in accordance with those directions. There is no record of any scheme member having given any such directions but the arrangements plainly contemplated, and all concerned effectively agreed, that the Properties would be immediately contributed by the Trustees to the WJL LLP. We consider further the nature of a scheme member's interest in paragraphs 51 to 53 below.

37. Clause 13(i) provides that a quorum of two Trustees is sufficient for a meeting of the Trustees and Clause 13(ii) provides that a meeting of the Trustees shall be deemed properly constituted if notice of the meeting is given to each of the Trustees at least seven days before the meeting and a quorum is present at the meeting. Clause 13(iii) allows the Trustees to pass a resolution without meeting provided that all Trustees sign a copy of the resolution. In this respect, Trustees' meetings may not have been preceded by any formal notice (we saw none) but the Trustees' resolutions that we saw were signed by all the Trustees.

38. Clause 15 requires the preparation of annual accounts and requires the Trustees to provide a copy of the accounts to each Member and the Trustees also "*shall at that time provide each Member upon request with a valuation of his interest*". NSP said that the annual accounts had been provided to scheme members by hand and given that the only scheme members were also Trustees that is perhaps unsurprising. No scheme member requested a valuation of his interest, but as the Appellants' case is predicated on the basis that no scheme member had any vested interest in the WJL FURBS, this is also unsurprising. NSP was asked whether the Trustees had received any complaint from scheme members about the Trustees' choice of investment given its fall in value. He said there had been no complaint because nothing had been allocated to scheme members. The only scheme members were of course trustees and we suspect any other employee who might have been eligible for membership would have known little or nothing about the arrangements. There was no evidence of any communication to employees generally about the establishment of the WJL FURBS.

39. Schedule 1 to the Trust Deed contains a list of definitions, of which perhaps the most important are the definitions of "Member" and "Interest". A "Member" is any person who has been admitted to membership of the Scheme in accordance with the Scheme Rules and whose membership has not been terminated in accordance with the Rules. "Interest" means:

> "in relation to any Member that part of the monies and other assets of the Scheme at the date on which such interest is to be determined as the Trustees shall decide to attribute to those contributions paid by the Member and by the Employer on his behalf during any period of his membership of the Scheme."

40. That apart, "Normal Retirement Date" means the date notified to a scheme member in writing by his employer on his admission to membership "*or any other date which is subsequently notified*". We saw no evidence that any of the scheme members were notified of their normal retirement date at any stage apart from a curiously worded letter of 12 October 2006 regarding DJM's award under the WJL FURBS (see paragraph 75 below). From their applications for membership, however, we can see their respective ages at the time: NSP was 39 years old, DWSL was 37, JBL was 65, VAL was 57 (and apparently not in good health) and DJM was 63 years old.

41. The Scheme Rules are set out in Schedule 2 to the Deed. Rule 1 deals with membership and provides that, "*At the discretion of the Employer, any Employee may be invited to apply for membership of the scheme*". An employee that takes up that offer must then submit an application form to the Scheme Administrator. This is what the Appellants did (see paragraph 14 above) even though NSP seems subsequently to have forgotten or not known that they had (see paragraph 17 above). An individual ceases to be a scheme member on death, on leaving service and receiving benefits or on the assets representing his interest being transferred to another retirement benefits scheme.

42. Rule 2[a] deals with contributions. Each scheme member is required to contribute at the rate (if any) determined by the Company and notified in writing to the scheme member. No required contribution rate was notified to any of the Appellants. Scheme members are also entitled to make voluntary contributions "*to secure additional benefits*". None were made. Each employer may also pay contributions "*in respect of the Members in its employ*", the amount and timing of those contributions to be decided by the employer. We note that both the Trust Deed (in Clause 5) and the Scheme Rules in Rule 2 appear to envisage that contributions are made in respect of or on behalf of "Members", who are (by definition) only those employees who have been admitted to membership and whose scheme membership has not been terminated (see paragraph 39 above).

43. Rule 2[a][iii] provides that—

> "The Trustees shall agree with each Member which part (if any) of the contributions payable by or on behalf of him shall be paid for the sole purpose of providing any of the benefits described in Rule 8[b] payable in the event of death in service which part (if any) shall be paid for the benefits in Rule 8[c] and which part (if any) shall be paid for the purpose of providing him with a pension or cash sum retirement benefit."

44. We saw no such agreement between the Trustees and any of the Appellants as scheme members. Rule 13[i] requires the Scheme Administrator to provide each scheme member with written details of the Scheme and a notice of contributions to be paid by and in respect of him "*and the nature of the benefit to be provided therefrom as agreed with him in accordance with Rule 2[a][iii]*". The Scheme Administrator provided no such written details. On the basis that none of the Appellants made any contribution and that the Appellants' case is that the Company's *in specie* contribution was not made on behalf of any particular one of them, the absence of any written record is again unsurprising. There also appears, however, to have been no written

agreement regarding the cash contributions even though these were specifically allocated to the Appellants.

45. Rule 2[b] deals with "Benefits" and paragraph [i] provides that the benefits are limited to those provided for under subsequent rules. Paragraph [ii] provides that "*each Member's interest shall be applied in full to secure such benefits in respect of him as the Trustees shall after consulting the Member decide and notify to him*". We saw no documentary evidence of any consultation, decision or notification beyond what we record in paragraphs 74 and 75 below. Where the benefit takes the form of a pension, paragraph [iii] permits the Trustees to apply the assets attributed to the scheme member's interest in purchasing an annuity.

46. Rule 2[b][iv] provides that a scheme member "*who becomes entitled to benefits as aforesaid*" can make a written request to the Scheme Administrator before any benefit becomes due requiring the Trustees to transfer assets to another pension scheme in accordance with Rule 12[b] in lieu of all other benefits under the WJB FURBS. Alternatively, under paragraph [iv] a scheme member can require the Trustees to apply the member's interest in purchasing an annuity with an insurer of the member's choice. Rule 12[b] (read apart from Rule 2[b][iv]) gives the Trustees the power "*in their absolute discretion*" but subject to the scheme member's consent, "*to pay an amount equal to the Member's Interest*" to another pension scheme.

47. Rule 2[b] therefore contemplates that a scheme member must have a Member's Interest to be entitled to benefits under the Scheme and that his Member's Interest will be applied to secure those benefits and, if he directs, can be used by way of transfer to another pension scheme or in the purchase of an annuity from an insurer of the scheme member's choice.

48. Rule 2[b][iv][c] (which, we think, is wrongly numbered due to a formatting error and should just be numbered Rule 2[c]) provides that the Trustees shall (as they think appropriate), "*require a valuation of the assets of the Scheme and the interest of the (sic) each Member under the Scheme and to report (sic) in writing thereon to the Members*". We saw no evidence of any valuation or report being prepared.

49. Rule 3 provides for a scheme member's entitlement to a pension on his Normal Retirement Date. It is in the following terms—

> "… a Member will become entitled on his Retirement on his Normal Retirement Date to a pension provided from such part of his interest as shall be allocated to provide him with pension benefits subject to the provisions of Rule 6 and 7 the amount of the pension shall be determined by the Trustees."

50. Rule 6[a] deals with cash sum retirement benefits. It allows a scheme member to elect by notice in writing to the Scheme Administrator before retirement that, "*part or the whole of his interest be used to provide him with a cash sum benefit at such time as benefits under the Rules are payable*". There was no documentary evidence of any such elections being made. Rule 6[b] allows the Trustees to commute any pension that on the first payment date "*does not exceed the such (sic) minimum amount as the Trustees shall from time to time determine*". We saw no evidence of any such minimum amount being determined. Rule 7 allows a scheme member to elect in

writing that part of his interest be used to provide benefits for his spouse or dependants. Rules 4 and 10 deal with early retirement benefits and benefits on ceasing to be employed by a Scheme Employer. Rule 5 deals with benefits where a scheme member remains employed after his Normal Retirement Date and Rule 8 deals with death benefits.

51. As appears from the extracts that we have reproduced the drafting of the Trust Deed and Rules leaves something to be desired. Nevertheless, the basis on which the Deed and Rules are designed to work seems tolerably clear—

> (1) An employee must be invited to join the WJL FURBS as a scheme member and must accept that invitation by applying (Rule 1[a]).
>
> (2) As a scheme member he becomes entitled to the benefits so far as they are provided for him under Rules 3, 4, 5, 6, 7, 8 and 10 (Rule 2[b]).
>
> (3) The benefits to which a scheme member is entitled are those provided by his "interest". The definition of "interest" is therefore important and we set it out again, adding our own emphasis:
>
> > "in relation to any Member that part of the monies and other assets of the Scheme ***at the date on which such interest is to be determined*** as the Trustees shall decide to attribute ***to those contributions paid*** by the Member and ***by the Employer on his behalf*** during any period of his membership of the Scheme."

52. As the definition indicates, the Scheme monies and assets only have to be attributed to a particular scheme member's interest when it is necessary to do so. The Deed and Rules are not always precise as to when it is necessary to do so. At Normal Retirement Age a scheme member becomes entitled to a pension "*from such part of his interest as shall be allocated to provide him with pension benefits*". Thus it appears that if the Trustees have made no earlier allocation of the monies or other assets of the Scheme to a particular individual, they must do so on his Normal Retirement Date; the amount to be allocated being that part of the monies and assets at that time as the Trustees decide to attribute "*to those contributions paid by the Member or by the Employer on his behalf*". The contributions must also have been paid during his period of scheme membership; perhaps a natural corollary of contributions only being made by or in respect of scheme members (see paragraph 42 above).

53. As this indicates, a scheme member's interest is determined by the contributions that he has made or which his employer has made on his behalf. This is no doubt why the Trust Deed provides in Clause 5 that the Company "*shall keep a record of the contributions that have been made <u>on behalf of each Member</u>*" (our emphasis). Subject to our point in paragraph 54 below, prior to a time at which an immediate entitlement to benefits vests or the Trustees otherwise decide to allocate assets, it seems that no scheme member can ordinarily point to particular monies and assets held by the Trustees as the monies or assets to which he is entitled for the provision of his benefits. A scheme member's interest in the overall trust fund is dictated, however, by whatever contributions he has made or have been made on his behalf. A scheme member's interest depends upon the attribution of particular contributions to

that member. Without that attribution a scheme member has no interest and can only have an interest to the extent of that attribution.

54. Clause 6(iii) of the Trust Deed raises an issue because it contemplates that the Trustees shall invest all or part of a scheme member's interest in accordance with written directions from that member. Thus, on receipt of written directions, it appears that the Trustees would have to identify the Scheme monies or assets as they attribute to the contributions paid by or on behalf of the scheme member concerned and invest them for the future as he has directed.

55. While noting that point, we do not think that we need reach a conclusion on it or necessarily grapple with all the drafting difficulties and deficiencies presented by the Trust Deed and Rules. It presents no difficulty where particular contributions are made (as the cash contributions in this case) and the relevant scheme member directs how the amount contributed on his behalf is to be invested. Unsurprisingly, given the Appellants' case, we saw no evidence that any of the Appellants issued written directions to the Trustees as to the investment of any contribution made by or on his behalf. Obviously, however, as we have already noted, the Appellants always contemplated that the WJL FURBS would immediately invest the Company's *in specie* contribution of the Properties in WJL LLP. More generally, the Trust Deed and Rules would plainly work tolerably well in circumstances in which specified contributions are made in respect of specified employees and the WJL FURBS is administered on a basis that allows one to identify scheme members' interests. One of the issues that we have to resolve in this case is how the WJL FURBS is supposed to operate in a case in which it is acknowledged that the Company has made a contribution to the Scheme but it is said that the Company has not made its contribution on behalf of any particular scheme member (indeed, has deliberately refrained from doing so).

56. Rule 14 allows the Trustees at their discretion and without reference to the scheme members to amend the Trust Deed or Scheme Rules provided written notice is given to scheme members. We were told of no such amendments and saw no notice to scheme members of any such amendments. Finally, Rule 15 allows the Company to terminate the whole or any part of its contributions to the Scheme on 14 days' notice to the Trustees, Scheme Administrator and scheme members. In that event the Scheme assets may be transferred to another retirement benefits scheme, dissolved or continue to be held by the Trustees subject to the Rules.

The reasons for establishing the WJL FURBS

57. HMRC was anxious to establish precisely why those concerned had chosen to take these steps to establish the WJL FURBS. We consider in due course whether and to what extent (if at all) the reasons for establishing the WJL FURBS are relevant to the issues we have to decide. At this stage we record the evidence and set out our findings based on that evidence.

58. HMRC's request for copies of all minutes and/or notes of meetings, whether formal or informal, relating to the establishment of the WJL FURBS, and the awards under it, was answered in correspondence as follows:

> "Due to the rushed nature of the reorganisation of the W J Law Group the vast majority of decisions were made "on the hoof". There is virtually nothing of the decision making process nor the actual decisions recorded in writing either by a minute, e-mail or fax. Brian [JBL], Bertie [VAL], Dan [DJM], David [DWSL] and I [NSP] operated out of each others [*sic*] pockets during this period and still work without resort to minutes."

We observe that this statement does not deny that decisions were taken: just that any decisions were not necessarily recorded in any formal way.

59. Mr Rivett proceeded to cross-examine NSP in some detail about the decision to establish the WJL FURBS. NSP was responsible for financial matters and the other directors looked to him in respect of such matters. He had, in effect, been the person who had explained to the other directors what the FURBS arrangement was about (so far as he understood it). NSP said that the idea of a FURBS derived from a chance meeting with a friend of DWSL in a restaurant where DWSL and he were having dinner following a land valuer's Christmas party. At the restaurant they had met Alan Pink of Alan Pink Tax and Mr Giles. This had led to contact with QED, which had proposed establishing a FURBS and the LLP.

60. A Business Strategy Report of March 2006 prepared by QED ("the QED Report") suggested that the directors of the Company should consider restructuring the company's business as a limited liability partnership with JBL, DWSL and NSP as members and setting up a FURBS "*to provide an inheritance tax efficient method of building up pension funds for the beneficiaries of the FURBS including Brian Law who is looking to retire in the near future*".

61. The QED Report is dated after the initial steps to establish the WJL FURBS but in our view it is plain from the content of the Report and from NSP's evidence that the initial steps on 23 February 2006 were taken pursuant to the arrangement proposed by QED and eventually recorded in the QED Report. The letter of 16 March 2006 (see paragraph 22 above) was addressed to QED (and apparently copied to ACP) and enclosed the signed Trust Deed and signed "Client Agreement", which we consider to be QED's engagement letter of 13 March 2006 (although NSP was unable to recall whether this is what it was referring to). It was QED that had supplied ACP with the membership details for JBL, VAL and DJM on 10 March 2006 (see paragraph 13 above).

62. Mr Rivett put to NSP whether the documents were in fact entered into on the dates that they actually bore. He said that they were, although at this distance from events he could not recall the precise order of events other than from looking at the documents. We have no reason to think that the documents were wrongly dated. They are consistent with QED proposing the arrangement and the steps being taken pursuant to that proposal even though QED's engagement letter was only signed after the initial steps and the QED Report recording matters was only finally produced in March 2006. We therefore find that the documents establishing the WJL FURBS are correctly dated and correctly record what was done (subject to one issue concerning the Company's minute establishing the WJL FURBS (see paragraph xx below).

63. The QED Report noted at paragraph 3.10 that:

> "Brian Law is soon to retire from W J Law Group Limited and the directors have asked QED tax consulting to consider what provision can be made to provide for Brian Law in his retirement together with suitable succession planning strategies to deal with the ownership of the existing business post his retirement."

64. The QED Report went on to recommend a new business structure using an LLP, the members of which would comprise JBL, DWSL, NSP, the Company and the FURBS. It proposed that the Company would retain existing projects while the LLP would undertake new projects. The QED Report expressed the view that while contributions to a FURBS were deductible for corporation tax purposes they were not taxable on the individual FURBS members, provided the contribution *in specie* was not ear-marked for the benefit of a particular beneficiary. It accordingly proposed that a FURBS be created and a cash sum be contributed: specifically £10,000 each for JBL, DWSL and NSP and £2,000 each for VAL and DJM. It then proposed that the Company contribute development land *in specie* to the FURBS. The QED Report continues at paragraphs 8.8 and 8.9:

> "It is planned that the FURBS will introduce the development land into the W J Law & Co LLP in return for a balance on its capital account equal to the market value of the land. The LLP will use this land in the course of its business and the FURBS will be entitled to receive an income profit share from the LLP resulting from the building and sale of residential dwellings on the land. The FURBS will be able to draw against its capital account in the LLP as and when beneficiaries of the FURBS retire. This event will be subject to there being sufficient cash available in the LLP."

The QED Report set out a variety of commercial and tax benefits that it suggested could be derived from these arrangements.

65. In cross-examination NSP sought to emphasise what he claimed were the commercial benefits that he said lay behind the establishment of the WJL FURBS – the benefits of attracting and locking in key staff, strengthening the Company's balance sheet, the potential for tax saving by the Company. The first of these – 'locking in' key staff – was based in particular on what he said was his own experience having regard to his pension arrangements with the Company. Mr Rivett asked NSP about these arrangements but we had no details of them. The Company's accounts indicate that the company operated a defined contribution scheme in respect of the directors and employees and that the scheme and its assets were held by independent managers. NSP was clear that he saw his responsibility as a trustee of the WJL FURBS as owed to future staff. The fact that no other staff had ever been appointed as members of the WJL FURBS was because, as matters turned out, they were never in a position to bring anyone else in.

66. NSP said that he had not been the point of contact for the various professionals (accountants, solicitors, land valuers) needed to implement the arrangement. This had been handled between the Company's accountants and auditors, Mr Pink and QED. He denied that the whole arrangement was designed with JBL's impending retirement in mind and claimed that when the idea was first discussed JBL was not intended to be a member of the WJL FURBS, but that this had changed as matters

developed. We should say immediately that we do not accept NSP's evidence regarding JBL's retirement and his participation in the Scheme. It seems to us that the arrangement was designed with JBL's retirement in mind and that it was therefore always intended that he should participate. NSP also denied that the whole arrangement was tax driven and was part of a tax avoidance scheme and that that explained what Mr Rivett suggested was the substantial fee that the Company had paid QED for their advice. NSP said that all the directors thought that QED's fee was high but accepted that the tax saving involved covered it.

67. NSP confirmed that as the director responsible for the Company's financial affairs he would usually authorise letters written on the Company's behalf by its accountants and that his responsibilities included the Company's accounts. In this connection Mr Rivett took him to the Company's accounts for the year ended 31 March 2006, where the value of the Properties contributed to the WJL FURBS was recorded as in respect of Directors' pension costs. NSP said that the Company's accounts did not reflect the intention that lay behind the establishment of the WJL FURBS: they reflected the fact that in the period in question the only scheme members were the directors. Mr Anthony Glover of the Company's accountants had also sought in correspondence with HMRC to justify a deduction for QED's fees because (as Mr Glover put it in correspondence) QED had been instructed to "*find ways to remunerate the directors for the considerable business success they had achieved*". NSP did not recall the letter in question. Mr Glover in evidence said that the letter was based on information supplied by NSP. NSP, however, denied that the contribution of the Properties to the WJL FURBS was paid for the benefit of the directors.

68. NSP was clear that the WJL FURBS was established for good commercial reasons, even allowing for the tax saving it generated for the Company. JBL and DWSL in their evidence supported the reasons that NSP had advanced, in particular to retain and attract good staff and expanding the Company's balance sheet. JBL accepted that no other staff had been invited to become scheme members but denied that there was no intention to do so. He said it was always possible and the establishment of the WJL FURBS offered the opportunity to do so. It was one of the ways of and part of the plan for taking the business forward.

69. DWSL indicated that his main responsibility within the Company was 'operational' (identifying developments and house building) rather than financial and that he derived his understanding of the arrangements from NSP. He (as also JBL) referred to strengthening the Company's balance sheet but, like NSP, was unable to explain in what way the establishment of the WJL FURBS strengthened the Company's balance sheet.

70. DWSL confirmed NSP's account of how they were put in touch with QED (see paragraph 59 above) but said that he had not been particularly involved in the establishment of the WJL FURBS; NSP had explained the bare bones of the arrangement and it had sounded a good idea. DWSL was unable to recall any detail but he said that the ability to reward good staff was a key factor. He recalled that the tax benefits had been explained although he could not remember the detail. He had signed documents when asked to do so but did not recall specific meetings or events connected with establishing the WJL FURBS. He had not dealt with Mr Pink. He

had just told others to go ahead with the arrangements. He was not otherwise closely engaged in the establishment process.

Our conclusion on the reasons for establishing the WJL FURBS

71. We do not accept in its entirety NSP's and the other witnesses' evidence regarding the reasons for establishing the WJL FURBS. Our conclusion is that the reason for establishing the WJL FURBS can be found in the QED Report. We have previously set out paragraph 3.10 of the Report (see paragraph 63 above). Paragraph 6.18 notes that, "*A key commercial issue for W J Law Group is the impending retirement of Brian Law. This has presented the business with the issues of how to fund Brian's departure and how to plan the successor business*". Retirement and succession issues within a business may clearly be commercial issues. Tax considerations, however, frequently drive how those issues are dealt with.

72. The QED Report deals with a number of issues, and not just the FURBS, but in so far as the retirement planning element was concerned we think that funding JBL's 'retirement' in what was thought to be a tax efficient manner was the key consideration. Tax planning and not commercial considerations as such was the driving force. We refer to 'retirement' because paragraph 8.4.10 of the QED Report noted that the person 'retiring' can continue to be involved in the business in another capacity, for example as partner, which JBL was as a Member of the WJL LLP.

73. Possibly all concerned may have thought that in general terms, all being well with the business over time, the WJL FURBS would remain in existence and it would therefore be open to extend membership to anyone else who became a director and/or was a key player in the business. We consider, however, that the establishment of the WJL FURBS was directed principally to the issue of funding JBL's 'retirement' and that the only persons that anyone then envisaged would be eligible for and would become scheme members were the Appellants. None of the witnesses could explain how the arrangement would strengthen the Company's balance sheet. Apart from reducing the Company's tax bill, the point that underlies this is possibly that, looking at the group business as a whole, DTZ's original valuation of the Properties enabled WJL LLP to negotiate increased borrowings from the bank (a point to which we refer starting at paragraph 83 below).

The payment of benefits by the WJL FURBS and subsequent events

74. On 25 September 2006, the WJL FURBS made two retirement payments: £150,000 to VAL and £3,000,000 to JBL. The two letters confirming the awards and addressed to ACP indicated that the sums in question had been paid, although this does not appear to have been correct at the time.

75. A letter dated 12 October 2006 and addressed to DJM recorded that JBL, DWSL, DJM and NSP had agreed that the WJL FURBS should pay DJM £250,000 on his retirement (or death in service), as "*a full and final settlement on the W J Law FURBS and all W J Law Companies*". This agreement replaced "*any and all previous agreements*". The letter addresses the issue of retirement dates, indicating that:

> "In January 2007 we will meet to discuss retirement in the eighteen months ahead. All parties will have the ability to agree retirement in June 2008. This will ensure an initial impending retirement notice period of eighteen months. In January 2008 (and annually thereafter) an impending retirement notice period of twelve months will apply"

The payment was only made in August 2008 (when DJM was 66 years old). On 10 November 2008 JBL, DWSL and NSP confirmed to ACP that no further benefits would be paid to VAL or DJM from the WJL FURBS. No similar confirmation appears to have been given in respect of JBL.

76. ACP resigned as a trustee of the WJL FURBS on 13 November 2006 but remained the Scheme Administrator. According to NSP ACP resigned by agreement in order to save professional fees. We do not accept this. It may be that ACP had some concern that it was not being kept sufficiently informed on WJL FURBS' matters but the immediate cause appears to have been that the Northern Bank required some form of guarantee from the WJL FURBS (probably as a Member of the LLP), which ACP was not prepared to sign as a trustee. We assume that the Appellants as the continuing Trustees entered into the guarantee and that this may be what is referred to in the WJL LLP's accounts in later years (see paragraph 32 above).

77. The Company was expelled from membership of the WJL LLP on 15 March 2010 with immediate effect because it was "*guilty of conduct likely to have a serious effect upon the business*". On 5 June 2012 the LLP expelled the WJL FURBS from membership with immediate effect also because it was "*guilty of conduct likely to have a serious effect upon the business*". This appears to have arisen from the failure by the WJL FURBS to pay the sum of £276,034, being the overdrawn amount of its capital account. It is unclear precisely how or when this overdrawn amount had arisen.

78. On 8 January 2013 the Company notified the Trustees that pursuant to Rule 15 it would make no further contributions to the WJL FURBS. On 9 and 10 January 2013 the relevant parties to the WJL FURBS were notified that it was insolvent. Mr Glover of McGreery Turkington Stockman gave evidence to that effect. On 16 January 2013 the Trustees resolved to dissolve the WJL FURBS and on 18 January 2013 the Respondents were notified that the WJL FURBS had been dissolved.

The basis for the payment of benefits by the WJL FURBS

79. Before considering the basis on which payments were eventually made from the WJL FURBS, we note some points relating to the transfer of the Properties to the WJL FURBS and the WJL FURBS' contribution of the Properties to WJL LLP.

80. NSP and DWSL jointly instructed DTZ to value the Properties at 31 March 2006. NSP's evidence was that at the time the contribution was made, the Board believed (on the basis of DTZ's valuation) that the Properties were worth £10,325,000. Having regard to DTZ's later lower valuation and his knowledge of the property market, he considered that the initial valuation was excessive. The Properties appeared at a cost in the Company's accounts of £3,236,577.

81. DWSL and NSP both said that there were no formal Trustees' meetings. They were asked as to the appropriateness of the WJL FURBS investing its assets in an LLP. DWSL said that it was not clear at the time that it was an unwise investment. NSP accepted that it had proved to be an unmitigated disaster and a mistake. Nevertheless, he said that he had believed that it was the best thing to do at the time.

82. As regards the question of any benefits to which the Appellants, as members of the WJL FURBS, might have been entitled at the outset:

(1) NSP's evidence was that at the time of the *in specie* contribution, there was no explicit or implicit, oral or written allocation of the contribution by the Company or the Trustees. At no time apart from when payments were actually agreed to be made to JBL, VAL and DJM (see paragraphs 74 and 75 above), was any other value intended or earmarked to secure benefits for any particular employee or employees. The intention was that the fund should be held as a "pool" to incentivise current and future employees and directors of the company.

(2) JBL's evidence was that while it was in contemplation that payments would be made from the WJL FURBS to himself and to two others on their retirement in due course, the contributions were not earmarked in any way for particular scheme members. It was only at the later date that JBL and his co-trustees approved lump sum payments to JBL, DJM and VAL out of the WJL FURBS on their retirement. He said that the understanding was that after those payments had been made they would receive no further benefits from the WJL FURBS. No further consideration was given as to what benefits, if any, would be paid out and it was certainly not in contemplation that any particular individuals would or would not be benefitted.

(3) DWSL's evidence was that when the contributions were made, it was left entirely open as to who would receive benefits on retirement out of the fund, when and in what amounts. Mr Rivett challenged him in cross-examination on this statement on the basis that his recollection of this detail was inconsistent with his claimed general lack of knowledge and understanding of the arrangement when it was set up. DWSL said that it was only at the later date that DWSL and his co-trustees approved lump sum payments from the WJL FURBS to JBL, VAL and DJM on their retirement. No other proposals had been made around the time of the contribution or subsequently to allocate any benefits to any other actual or potential beneficiaries.

(4) Mr Green, a director of ACP, confirmed in evidence that in February 2006 ACP had received cash contributions as follows: £10,000 for each of NSP, DWSL and JBL and £2,000 for each of VAL and DJM. He said that ACP was aware of the *in-specie* contribution. At no point had ACP been notified of any allocation of the *in-specie* contribution to particular scheme members.

83. NSP alluded to the fact that a certain amount of work had had to be undertaken to get the Company's bank on board with the new arrangements. NSP said that the bank facility was key to the whole matter because that would dictate whether a cheque for

£3,000,000 could be written in favour of JBL. In this regard we were provided with very little documentation or evidence to explain the bank funding or to throw light on whatever negotiations with the bank were needed to implement the arrangement.

84. NSP said that there was a verbal agreement with the bank in the week before 31 March 2006 to accept the new structure. It appears that there was some difficulty in explaining the new structure to the bank and getting its legal department's agreement to the arrangements, presumably having regard to ensuring on-going security for the bank's lending. NSP said, however, that there was agreement in principle with the bank in March 2006. NSP was unable to recall the detail of what had then transpired regarding the release of any security over the Properties and its replacement by new security. In due course, we have noted that cross-guarantees appear to have been put in place to include the WJL FURBS (see paragraphs 32 and 76 above) but there was no clarity on these matters.

85. While the negotiations with the bank in February/March 2006 leading to the reorganisation might have been conducted at face-to-face at meetings, we would have expected the matter to have been recorded in some way at some time in writing, but neither party produced anything to assist us on this. We think it is reasonable to assume that the Properties were subject to whatever security the Company's bank had over its assets prior to 31 March 2006 and what might then have had to be negotiated would be for the Properties to be released from that security (if in fact that was necessary) and for them to be brought back into the bank's security once vested in WJL LLP, either immediately or in due course when WJL LLP increased its borrowings.

86. One aspect of the arrangements was that the Properties had a recorded cost to the Company of £3,236,577 but the contribution to the WJL FURBS was supported by DTZ's valuation of £10,325,000. It seems that the WJL LLP may have been seeking to increase its borrowing by reference to the current valuation of the Properties, and we can see from the accounts that there was an increase in bank loans. NSP said that the bank was an integral part of the arrangement because cash was needed to provide liquidity – not least to facilitate payments from the WJL FURBS. He said that this had been sorted out before September 2006 and also indicated that the increase in bank borrowing that was achieved allowed funds to be applied to fund expansion in the Republic of Ireland.

87. Plainly the QED Report contemplated that the WJL FURBS would be able to fund retirement payments by drawing against its capital account in the LLP as and when beneficiaries of the FURBS retired. As QED noted, however, this would be subject to there being sufficient cash available in the LLP (see paragraph 64 above). If the WJL LLP was not generating sufficient free cash resources from its activities, the obvious solution would be to replace Members' contributions by borrowing, as the WJL LLP's accounts suggest may have been the case. Without any detail of the bank funding, we are unable to say whether it would in fact cast any light on the arrangements starting with the establishment of the WJL FURBS and ending with the payments to JBL, VAL and DJM.

88. The letter of 25 September 2006 to ACP recording the payment also stated that the payment had been made. In cross-examination JBL suggested that he received a

cheque for £3,000,000 but he had to await Mr Green's signature as the final trustee on the Trustees' Resolution. It seems that payment was in fact only made at the end of November 2006. JBL had no precise recollection of when he actually received the cheque or when it was actually paid. The letter was signed by ACP but as ACP was not represented at the meeting its signature was presumably obtained after the event. JBL suggested that Mr Green had been slow in dealing with the matter. In re-examination by Mr Sokol QC JBL clarified that payment had in fact been made by direct bank transfer so that the cheque had never been paid and had instead been destroyed. NSP's evidence had always referred to the use of a cheque as the means of payment. In whatever way the amount was paid, JBL said that he reinvested the money in WJL LLP and it appears that this may always have been intended. Whether this was part of the arrangement with the bank is unclear.

89. There was some discrepancy in NSP's and JBL's account of the Trustees' meeting that was supposed to have taken place on 25 September 2006 to approve the payment to JBL. NSP said that it had taken place at VAL's house. JBL said that it was held in the board room of the house in Lisburn where he had been born, but recalled going to VAL's house after the meeting.

90. Mr Rivett suggested to JBL in cross-examination that the Trustees' Resolution of 25 September 2006 was unusual: it stated that the amounts had been paid, when they had not; it purported to record a Trustees' Resolution in a formal manner, when everything else the Trustees had done was not so recorded; and there was a divergence of evidence between himself and NSP as to the detail of the meeting that was supposed to have been held on 25 September 2006. Mr Rivett suggested that in fact all concerned had agreed from the outset that JBL would receive £3,000,000 and that the Trustees' Resolution could have borne any date. JBL denied that this was so and said that he was "fairly sure" that the resolution had been signed on 25 September 2006. He was also clear about the meeting at the board room in Lisburn and going to VAL's house afterwards.

91. As regards the figure of £3,000,000, NSP said that this had been settled on because it was 20 times the amount that was to be paid to VAL. He denied that the amount had anything to do with the value of the Properties or that the arrangement was to extract over £3,000,000 worth of land from the Company via the WJL FURBS as a precursor to passing the money to JBL even though the parties may have recognised that the reorganisation allowed for this possibility. He claimed that JBL had suggested £3,000,000 on the basis that at 20 times VAL's amount HMRC would then be more interested in investigating JBL than they would VAL. Mr Rivett suggested that this was not credible but NSP insisted it was the truth of the matter.

92. We see no need to comment on whether this last point was really a thought that might have been in NSP's, JBL's or anyone else's mind or expressed at the time. It also seems unimportant to conclude whether or not 20 times was the basis for deciding on the amount of JBL's and VAL's payments or whether there was some other basis for the decision to pay them these amounts. What seems clear to us, and indeed the object of the arrangement, was that land with a cost to the Company £3,236,577 should be extracted from the Company into the WJL FURBS, contributed to the WJL LLP and so far as necessary bank funding used to 'convert' the land into cash to make the payments to JBL and VAL that everyone had in mind. At all times

the parties concerned acted in conformity with the overall plan that had been put forward by QED and Mr Pink on the understanding that these steps would happen. JBL said that he could not recall precisely how the figure of £3,000,000 had been decided upon. He suggested that it seemed and that they were advised it was an appropriate figure. It had "come together" in consultation with the advisers. He was clear, however, that the decision had been taken on or around 25 September 2006.

93. We have no reason to think that there is any significant issue about the dating of the Trustee's Resolution or the meeting, which we can accept took place on or around 25 September 2006. We think that it is immaterial whether or not ACP knew about the meeting in advance because it signed the letter when presented with it and the letter therefore becomes a valid Trustees' Resolution. The important aspect is that this was, as we find, just the next step in a preconceived arrangement that started with the establishment of the WJL FURBS and was designed to lead to the extraction of payments in favour of JBL, VAL and DJM through the mechanism of the WJL LLP and the WJL FURBS. We consider in due course the consequences of our finding in this respect.

94. As regards the letter of 12 October 2006 promising DJM the sum of £250,000 on his retirement, we also conclude that this was part of the same overall arrangement as that which led to the payments being made to JBL and VAL.

Summary of our findings of facts

95. Piecing the matter together from the Appellants' evidence and the documents, we have concluded as follows—

(1) The arrangements were conceived in the period leading up to February/March 2006 and were executed thereafter as a single arrangement designed to achieve the following outcomes.

(2) The Company was to establish the WJL FURBS and contribute the Properties with a recognised cost of £3,236,577 to the WJL FURBS based on DTZ's original market valuation of £10,325,000.

(3) The WJL FURBS was to immediately contribute the Properties to WJL LLP at that valuation.

(4) The DTZ valuation would provide the basis for negotiating increased borrowing from the bank that would enable the WJL FURBS to be repaid its WJL LLP capital to the extent needed to fund payments to JBL, VAL and DJM on their retirement and to allow any excess to be employed for the benefit of the WJL group's business.

(5) On their retirement JBL, VAL and DJM were to receive payments from the WJL FURBS of £3,000,000, £150,000 and £250,000 respectively. The Trustees may not finally have determined (in the form of a written resolution or letter) to pay these amounts until the later dates but it seems to us (and we so find) that these amounts were in everyone's mind from the outset when the Company made its in specie contribution of the Properties to the WJL FURBS (at which point the arrangement appears to have been agreed in principle with the bank).

(6) DWSL and NSP obtained their interest in WJL LLP but the Appellants did not envisage that they would be entitled as part of these arrangements to receive any specific payments from the WJL FURBS. Given their age, this is not surprising.

96. No doubt, on the basis that the WJL FURBS had been created, if it remained in existence and flourished over time, it might have been possible to use whatever value remained in it to provide future retirement benefits to whoever were the scheme members from time to time, including NSP and DSWSL. That was not, however, the immediate purpose underlying its establishment. Furthermore, they were the only other scheme members at the time, whatever may or may not have been contemplated about the admission of other key employees.

The Legislation

97. At the relevant time, section 386 of the Income Tax (Earnings and Pensions) Act 2003 provided as follows—

386 Charge on payments to non-approved retirement benefit schemes

(1) A sum paid by an employer—

(a) in accordance with a non-approved retirement benefits scheme, and

(b) with a view to the provision of relevant benefits for or in respect of an employee of the employer,

counts as employment income of the employee for the relevant year.

(2) The "relevant tax year" is the tax year in which the sum is paid.

(3) Subsection (1) does not apply if or to the extent that the sum is chargeable to income tax as the employee's income apart from this section.

(4) But if, apart from this section, the payment of the sum would be a payment to which Chapter 3 of this Part (payments and benefits on termination of employment etc) would apply, subsection (1) applies to the sum (and accordingly that Chapter does not apply to it).

(5) In this Chapter—

(a) "employee" includes a person who is to be or has been an employee,

(b) section 5(1) (application to offices) does not apply, but "employee", in relation to a company, includes any officer or director of the company and any other person taking part in the management of the affairs of the company,

(c) "employer" and "employment" have the meanings corresponding to the meaning of 'employee' given by paragraphs (a) and (b),

(d) "director" has the meaning given by section 612(1) of ICTA, and

(e) "relevant benefits" has the meaning given by that section, and section 612(2) of ICTA applies to references in this Chapter to the provision of relevant benefits as it applies to such references in Chapter 1 of Part 14 of ICTA.

(6) For the purposes of this Chapter benefits are provided in respect of an employee if they are provided for the employee's spouse, widow or widower, children, dependents or personal representatives.

(7) Any liability to tax arising by virtue of this section is subject to the reliefs given under—

(a) relief where no benefits are paid or payable, and

(b) section 266A of ICTA (life assurance premiums paid by employer).

388 Apportionment of payments in respect of more than one employee

(1) If a sum within section 386 is paid for or in respect of two or more employees, part of it is treated as paid in respect of each of them.

(2) The amount treated as paid in respect of each employee is–

$$A \times (B \div C)$$

Where—

A is the sum paid,

B is the amount which would have had to be paid to secure the benefits to be provided in respect of the employee in question, and

C is the total amount which would have had to be paid to secure the benefits to be provided in respect of all the employees if separate payments had been made in the case of each of them.

392 Relief where no benefits are paid or payable

(1) An application for relief may be made to an officer of Revenue and Customs if—

(a) a sum is charged to tax by virtue of section 386 in respect of the provision of any benefits.

(b) no payment in respect of, or in substitution for, the benefits has been made, and

(c) an event occurs by reason of which no such payment will be made.

(2) The application must be made within 6 years from the time when the event occurs.

(3) The application must be made by the employee or, if the employee has died, the employee's personal representatives.

(4) If an officer of Revenue and Customs is satisfied that the conditions in subsection (1) are met in relation to the whole sum, the officer must give relief in respect of tax on it by repayment or otherwise as appropriate, unless subsection (6) applies.

(5) If an officer of Revenue and Customs is satisfied that the conditions in subsection (1) are met in relation to part of the sum, the officer may give such relief in respect of tax on it as is just and reasonable, unless subsection (6) applies.

(6) This subsection applies if—

(a) the reason why no payment has been made in respect of, or in substitution for, the benefits, or

(b) the event by reason of which there will ne no such payment,

is a reduction or cancellation of the employee's rights in respect of the benefits, or part of the benefits, as a consequence of a pension sharing order or provision.

(7) In subsection (6) "pension sharing order or provision" means any such order or provision as is mentioned in—

(a) section 28(1) of WEPA 1999 (rights under pension sharing arrangements), or

(b) Article 25(1) of WRP(NI)O 1999 (provision for Northern Ireland corresponding to section 28(1) of WRPA 1999).

The Appellant's submissions

98. Mr Sokol QC's submissions for the Appellants were straightforward: the WJL FURBS was discretionary, both as to membership and benefits. We observe that this is plainly correct as regards membership (see Rule 1[a], set out at paragraph 41 above). Mr Sokol cited Rule 2[a][ii] in support of his submission that entitlement to benefits was discretionary. This provides that "*Subject to the provisions of Rule 13[ii] each Employer shall pay to the Trustees contributions in respect of the Members in its employ. The amount and timing of employers [sic] contributions to be shall be [sic] decided by the Employer*." Again, we observe that this is correct so far as the amount and timing of employer's contributions is concerned (assuming no separate agreement, for example, as part of an employee's terms of employment). It leaves open the question of allocation (given that any contribution is made in respect of current scheme members and not prospective or future scheme members). It also leaves open the question of entitlement to benefits and the allocation of the FURBS' assets once any contribution has been made in respect of a particular scheme member.

99. He noted that the Company had 21 employees, five of whom were members and the rest were eligible to be invited to apply for membership. The Appellants were

members so that they, their widows and dependants and others "standing in relation to them" were eligible to benefit from the Scheme. He said that at the time that the Company contributed the land there had been no allocation of benefits beyond the cash contribution of £34,000. He submitted that the contribution of the land had not been made "with a view to the provision of relevant benefits for or in respect of an employee" as required by section 386(1)(b) ITEPA. That, put briefly, was the end of the matter for 2005/6. The position in later years was not in issue in these appeals.

100. Dealing with the apportionment provided for in section 388, Mr Sokol noted that section 386(1)(b) referred to "an employee" who was consequently "the employee" who is taxable in respect of the sum paid. Section 388 made it clear that there could be more than one employee but where there were several they still had to be distinguishable by reference to sums paid in order to provide benefits for each of them respectively. Thus, where there was no particular employee for whose benefit the sum is paid and no identifiable benefits to be provided, section 388 did not offer HMRC any solution: "B" in the formula referred to "the employee in question" and "C" referred to "all the employees if separate payments had been made in the case of each of them", neither of which was satisfied in these circumstances. Mr Sokol said that this conclusion was further supported by section 395, which operates via subsection (4) to remove from charge under section 394 any lump sum benefit where an employee had been assessed under section 386 (or its predecessor section 595 ICTA) on any contribution to the FURBS.

101. Mr Sokol criticised HMRC for seeking to exercise a general discretion to decide who of the possible ultimate beneficiaries under the WJL FURBS should be taxed and on what amount. In the present case he noted that several of the Appellants were charged in respect of sums that they had never received and now could never receive. If in fact that were possible Mr Sokol drew attention to relief under by section 392 and invited us to conclude such relief was available and to reduce the assessments to nil. (Claims for relief under section 392 had previously been submitted on behalf of NSP and DWSL on 21 June 2012.)

The Respondent's submissions

102. Mr Rivett's submissions for HMRC depended to an extent upon our findings of fact. We start by recording the various bases that HMRC put forward in their skeleton argument (which we summarised briefly in paragraph 8 above) to justify the closure notices and amendments. We then record Mr Rivett's oral submissions in closing which he based on the view that he said we should take of the evidence.

103. As regards the terms of the WJL FURBS, HMRC noted that the apparent effect of the Trust Deed and Scheme Rules was that the Trustees held the funds on trusts that envisaged that they could be distributed only in the form of 'relevant benefits' to scheme members. The effect of Rule 2[b][ii] (see paragraph 45 above) was that the Trustees were obliged to apply each Member's Interest in full to secure benefits on his behalf. That Rule envisaged that the Trustees should consult the scheme member and notify him of the benefits, which it was said referred back to Rule 2[a][iii] (see paragraph 42 above). HMRC also referred to the requirement in Rule 13[i] for the Scheme Administrator to notify contributions paid by or on behalf of a scheme member and the nature of the benefit agreed to be provided as a result. Necessarily,

HMRC noted that this had not been complied with. They noted, however, that the cash and *in specie* contributions were held on the same terms.

104. HMRC's primary case was that a portion of each of the *in specie* contributions was expressly or impliedly paid "in respect of" each Appellant at the time at which it was paid. In support of this contention HMRC relied on—

(1) The circumstances in which the WJL FURBS was established and in particular the fact that the Scheme was established as a tax avoidance scheme designed to exploit a perceived deficiency in section 386 ITEPA and the corporation tax regime;

(2) The coincidence in identity of the directors of the Company, the Trustees and the scheme members at the material time;

(3) The terms of the WJL FURBS and the Scheme Rules;

(4) The sums that certain of the Appellants in fact received from the Scheme shortly after the *in specie* contributions were made and the terms on which those relevant benefits were received.

105. HMRC also made the point that the burden of proof lay with the Appellants. In the event that the Appellants failed to demonstrate that a portion of each of the *in specie* contributions were not expressly and/or impliedly paid 'in respect of' particular Appellants, then the Appellants' appeals against the closure notices could not succeed.

106. In the alternative, if there was in fact no express or implied payment of the *in specie* contribution for the benefit of a particular employee, HMRC said that the *in specie* contributions were nevertheless paid "in respect of" all the Appellants. HMRC relied on the Scheme Rules to support this submission on the basis that the scheme members could benefit from the trust property and the Appellants were the only scheme members. Section 388 explicitly recognised the possibility that a sum could be paid for the benefit of a number of employees and provided the basis for apportioning the sum between them. In particular, the numerator "B" should be the amount of express and/or implied allocation of the *in specie* contributions as between the Appellants. HMRC relied on the same four factors mentioned in paragraph 102 above in support of this contention.

107. Alternatively HMRC submitted that if neither of the previous bases provided the correct manner of proceeding, the *in specie* contribution should be apportioned equally between the Appellants. In support of this contention HMRC relied upon the following facts and matters—

(1) Under the Scheme Rules membership was open to any employee of the Company;

(2) At all material times the Appellants were the only scheme members;

(3) The Company's contributions to the Scheme were to be provided "*in respect of the Members in its employment*" (Rule 2[a][ii]);

(4) Under the Rules, the only purpose for which any contribution to the Scheme could be used was the payment of 'relevant benefits' to scheme members;

(5) In the absence of any express or implied allocation, it should be presumed that the intention was that the *in specie* contribution should be allocated between each of the scheme members equally (see *McPhail v Doulton* [1971] AC 424).

Thus, for the purposes of section 388(2), the numerator "B" would be an amount equal to a share of the *in specie* contribution if divided equally between each of the Appellants.

108. Mr Rivett submitted in support of these contentions that the Trust Deed and Rules contained no relevant discretion. If and in so far as the Trust Deed and Rules conferred upon the Trustees power to determine the size of a particular Member's Interest, there was an implied obligation on the part of the Trustees to exercise that power and an express obligation to notify each scheme member of his interest. On the basis that the Trustees failed to notify each scheme member of his interest, the only tenable inference (by analogy with *McPhail v Doulton*) was that the fund was to be held for members equally.

109. Finally HMRC submitted that the whole arrangement was a sham or other pretence. This was put forward on the basis that the evidence would show that the documentation produced did not accurately reflect the true nature of the Appellants' arrangements and that an ascertained proportion of the *in specie* contribution was allocated to each of the Appellants at or about the time that the Company made its *in specie* contribution to the WJL FURBS.

110. We would observe that we are unclear to what extent this submission really differs from HMRC's primary case that a proportion of the *in specie* contribution was *in fact* paid in respect of particular Appellants or its alternative case that although the *in specie* contribution was paid in respect of all the Appellants there was *in fact* an allocation to one or more of them. To the extent that there is some difference it may rest on the approach that HMRC were urging us to adopt to attribute the *in specie* contribution to particular Appellants: namely, to ask the question, "what was the substance and reality of the transaction entered into by the parties" (see *Audley v HMRC* [2011] UKFTT 219 (TC) at [43] and [44]) and to ignore the actual language used by the Appellants and to look at all the relevant circumstances, including the Appellants' subsequent conduct (see *Hitch v Stone* [2011] EWCA Civ 63).

111. In support of that contention HMRC relied on the following facts and matters—

(1) The circumstances in which the WJL FURBS was established and in particular the fact that it was established as a tax avoidance scheme designed to exploit a perceived deficiency in section 386 ITEPA and the corporation tax regime;

(2) The coincidence in identity of the directors of the Company, the Trustees and the scheme members at the material time;

(3) The terms of the WJL FURBS and the Scheme Rules and in particular the apparent failure of the Trustees and the Company to adhere to any of their obligations under the terms of the Trust Deed and Rules;

(4) The absence of any documentary records identifying the basis upon which decisions were made by the Company or the Trustees;

(5) The implausibility of the suggestion that an asset with the value of the *in specie* contribution would have been contributed to the Scheme without any agreement as to its allocation between scheme members at the material time;

(6) The timing of the various payments that were made from the WJL FURBS over the months following the making of the *in specie* contribution.

HMRC made clear that they were not alleging that the arrangements were fraudulent but that they did not in substance correspond to the terms of the written instruments upon which the Appellants sought to rely.

112. In his oral submissions Mr Rivett advanced two particular bases—

(1) Both cash and *in specie* contributions were plainly paid to provide relevant benefits and in fact there was an understanding as to who would get what, even though nothing was written down;

(2) As a matter of law and the construction of the relevant provisions, it was open to us to infer that the *in specie* contribution was allocated equally.

113. In support of his first submission Mr Rivett drew attention to various aspects of the evidence before us: the fact that the accounts recorded the *in specie* contribution as being made for the directors; NSP's failure to recognise the tax benefits underlying the arrangement; his failure to mention JBL's gift; the implausible explanation for VAL's £150,000; the divergent accounts of the 25 September meeting; the suggestion that ACP resigned as trustee to save fees. Mr Rivett said that the Appellants' assertion that there was no allocation at the time the Company made its *in specie* contribution depended upon documents and witnesses that had been shown to be unreliable. Mr Rivett nevertheless accepted that HMRC could point to no document that identified the actual allocation that was made but he suggested that the closure notice were as accurate an assessment of the position taking account of what had actually happened. To the extent that the closure notices had not taken account of JBL's £3,000,000 payment, they could be adjusted appropriately.

114. Turning to his alternative submission, Mr Rivett went through the Trust Deed and Scheme Rules, drawing our attention to the failure to comply with the requirement to notify interests and benefits. In this respect he noted that the failure was that of the Company in not telling the Trustees for whose benefit the *in specie* contribution was being made. He noted that the Company nevertheless had claimed a deduction for the *in specie* contribution as paid in respect of employees generally. He said that the Appellants could not get the best of both worlds: if the payment was made in respect of employees but was not specifically allocated to particular employees then it should be taken to have been paid in respect of them all equally.

The Appellants' submissions in reply

115. Mr Sokol QC replied on behalf of the Appellants. He repeated the point that there was no record relating to the *in specie* contribution because there was nothing to record. In the circumstances it would be bizarre if there had been some record. He rejected the idea that there was any sham; indeed, he said that it was unclear precisely what HMRC was alleging to be a sham. He said that NSP's evidence had been consistent as to the purpose of the WJL FURBS and that there was nothing to suggest that the quantum of any benefits received had been decided before they were paid. He rejected the suggestion that *McPhail v Doulton* represented any authority for allocating the *in specie* contribution equally among the Appellants.

Discussion

The 'tax avoidance' character of the arrangement

116. We start by rejecting any suggestion implicit in HMRC's submissions that the taxation consequences for the Appellants of these arrangements depend to any extent upon whether or not the arrangements amounted to "tax avoidance". HMRC's skeleton argument might be taken to suggest that the Appellants were to be damned if their arrangements could be so characterised (see in particular the summary at paragraphs 104(1) and 111(1) above). The fact that particular arrangements are entered into with the aim (even the sole aim) of minimising or 'avoiding' taxation is, however, irrelevant to the construction and application of particular statutory provisions unless those provisions incorporate some relevant 'motive' or 'purpose' test (which the current provisions do not). In the event we did not understand Mr Rivett to put the matter in that way.

117. The fact that the arrangements may have been devised to achieve a particular tax objective may nevertheless be relevant to the characterisation of the arrangements, or to their 'reality', and therefore in determining how particular statutory provisions, purposively construed, should apply to that reality. In the present case, however, what is more relevant in our view is what did everyone understand and agree as part of the arrangements, noting that the Appellants ordinarily conducted their affairs on the basis that decisions were not normally recorded in any formal manner even when taken.

The allocation of unallocated contributions

118. Our starting point is the Appellants' proposition that the Company contributed £34,000 to the WJL FURBS allocated between the Appellants as scheme members in the proportions 10:10:10:2:2 and then contributed £10,325,000 to the Trustees allocated to no particular scheme member. Thereafter, the Trustees exercised their 'discretion' to pay to each of JBL, VAL and DJM on their retirement lump sums of £3,000,000, £150,000 and £250,000 respectively.

119. There is no dispute (there could be none) that the Company's cash contributions on their behalf fall within and are taxed under section 386(1). That in itself represents HMRC's acceptance of the validity of the WJL FURBS. HMRC certainly have not asserted any other basis of taxation. Furthermore, we think that section 386(1) would

apply whether the Company paid £34,000 as a single sum or as five separate amounts. In other words, it is unnecessary to invoke the specific apportionment rule in section 388 where the amount that is paid to secure particular benefits in respect of each employee is specified.

120. We return to the function and operation of section 388 in paragraph 149 below. Our immediate observation in relation to the function and operation of section 386, based on the Appellants' argument, is similar to that of the Court of Appeal in *Irving v HMRC*. In that case Lord Justice Rimer observed (at [46]) that the form of the funding can make no rational difference to the taxing policy underlying the statutory provisions. As he continued regarding the suggested difference between cash and in specie contributions—

> "Further, if the distinction is in fact relevant, there could in some cases be a real uncertainty as to the side of the line on which the method of funding lay. In most cases the contribution proposed to be made by the employer for a particular year will be the subject of prior agreement with the scheme trustees. If, for example, an employer agrees to pay £100,000 and later agrees with the trustees that he will satisfy that commitment by transferring £100,000 worth of shares, will he be regarded as having 'paid' £100,000 pursuant to his commitment? Or will he be regarded as having simply made a transfer of non-cash assets? Whatever the answer, why should Parliament be interpreted as having intended such an enquiry to be embarked upon? What possible difference can it or should it be regarded as making?"

121. In the same way, the possibility that on Day 1 an employer can pay a small (taxable) sum to the trustees of a FURBS to secure the interest of employees to particular benefits from the fund and then on Day 2 pay the larger (non-taxable) sum actually required to fund those benefits would be as simple (and nonsensical) a way of negating the tax charge under these provision as the suggestion made on Mr Irving's behalf that the tax charge under section 595 Income and Corporation Taxes Act 1988 did not extend to *in specie* contributions.

122. The point that the Appellants seek to make would apply whether the later funding was in cash or kind. In either case, the sum paid by the employer to the trustees pursuant to the scheme to secure the benefits under the scheme would be paid "in accordance with" a non-approved retirement benefits scheme "with a view to the provision of relevant benefits". The only issue would be whether the sum was paid "for or in respect of an employee". This may depend upon the facts but plainly, as it seems to us, it must be possible (if section 386 is to operate) to attribute the payment or an identifiable part of the payment to a particular employee if one is to be able to say that the payment "counts as employment income of the employee for the relevant year".

123. As a general proposition, however, there seems no reason why a FURBS should have to operate on the basis that amounts paid by the employer to the trustees of the FURBS are always expressly attributed to a specific employee or specified employees. There may be scope for the employer to 'top up' the funding as appropriate: in other words, to pay an amount to the FURBS without specific

allocation of particular sums (or parts of sums) to particular employees. In this respect, our concern to some extent in this case has been the apparent inability of the Respondents to articulate as clearly as we might have expected how these taxing provisions are designed to operate in such cases. On the face of it there seems little sense in Parliament taxing specific contributions but leaving untaxed general funding.

The basis of the closure notices and amendments

124. We can understand that HMRC might wish to 'hedge their bets' in the present case depending upon the way in which the evidence emerged. On the other hand, the Appellants are appealing closure notices which are supposed to state the officer's conclusions and to make the amendments required to give effect to his conclusions. In each of the Appellants' cases, the stated conclusion is that "*the benefit in respect of an in specie FURBS contribution made by his employer has been omitted*". That much is clear. The closure notice continues, however, by stating the amendment that the officer is making to each Appellant's self-assessment return, including the statement that "I enclose an explanation of these figures". The explanation, however, is solely in terms of the overall computation and offers no explanation of the basis of computing the amount being added to employment income in respect of the *in specie* contribution.

125. Thus, in VAL's case, the "income from employment" is increased by £148,000 but the basis on which the officer has determined that this is the right figure to add is unexplained in the closure notice. For that explanation (such as it is) one has to revert to the letter that preceded the closure notice, being a letter of 14 August 2008, which explained as follows—

> "In accordance with the [*Irving* case], I will now proceed to issue closure notices in respect of the Directors;' enquiries for 2006 and make the appropriate amendments to their Self Assessments. The quantum of the amendments is shown in the attached computation. In the two cases where benefits have been paid out, I have taken those benefits as the value transferred into the scheme in total. Therefore any initial contribution is increased by a portion of the asset transfer to arrive at the total received from the scheme. The remainder of the asset value is then divided equally among the remaining three Directors."

126. This was the basis upon which the figures in the second column of the table at paragraph 2 above were arrived at. As part of his various written and oral submissions for HMRC Mr Rivett suggested that these figures should stand either because they were the best allocation that could be made in the circumstances or, alternatively, because the Appellants (on whom the burden of proof rested) had failed to satisfy us that some other basis applied. Neither of those suggestions commends itself to us in the circumstances.

127. Apart from anything else, they tax VAL and DJM by reference to the amounts that they received while ignoring the amount that was paid to JBL. This may be because the officer conducting the enquiry did not know (surprising as that may be) at the time at which he issued the closure notice that £3,000,000 had been paid to JBL. The other potential objection is that the allocation of the Company's *in specie*

contribution is driven by hindsight (by reference to the amounts subsequently paid out) rather than, as we would have expected, a principled application of the way in which HMRC considered the legislation should operate in the absence of any specific allocation. If HMRC themselves demonstrate some uncertainly as to the way in which the legislation is supposed to operate there is little hope for taxpayers in being able to submit accurate self-assessment returns.

128. What the officer certainly knew (having regard to his computation) as a result of his enquiries was that £34,000 had been paid on 16 March 2006 on behalf of the five scheme members, split in the proportions 10:10:10:2:2. On 31 March 2006 the Company made a further payment of £10,325,000. Looking at the matter at that point in time, which was the time at which the officer was contending the tax charge arose, one might have expected him to issue closure notices allocating the further payment in the same proportions. On that basis NSP, JWSL and JBL would be allocated £3,036,765 each and VAL and DJM would be allocated £607,352 each.

129. On the basis that the Appellants were contending that the Company had made its further payment of £10,325,000 to the WJL FURBS on an unallocated basis, we assume (although it is not explicit) that the officer was proceeding by apportioning the amount under section 388. To the extent that any payment is made in respect of more than one employee, where it is not possible on the facts to attribute any part of the payment as paid specifically for the benefit of a particular employee, section 388 specifies the basis of apportionment.

130. In this respect, "B" and "C" in the formula both operate by reference to "the benefits to be provided" and "in respect of the employee in question". This does not seem to us to be a formulation that is necessarily an easy matter to determine because it appears to require some assessment of the benefits to be provided and what would have to be paid to secure them. In this respect, the formula in section 388 is designed to allocate the sum paid with a view to the provision of relevant benefits for or in respect of two or more employees (amount "A" in the formula) but by reference to each employee's share of the total amount which would have had to be paid to secure the benefits to be provided in respect of all employees.

131. We think that section 388 is designed to address the issue of unallocated payments to FURBS but we are bound to note that HMRC's submissions did not adequately explain how the formula should operate in this case. Mr Rivett's closing submissions for HMRC were to the effect that the unallocated contribution should be divided equally between the Appellants. This was presumably (although we do not believe that Mr Rivett expressed it in this way) on the basis that the unallocated contribution should be taken to have secured identical benefits for each of the Appellants under the WJL FURBS, without the benefit of hindsight but notwithstanding the Company's different allocation of the cash contributions between the Appellants.

132. The closure notice appears to have proceeded on the basis that the benefits to be provided to VAL and DJM were the lump sum payments that they eventually received and that the amount that would have to be paid to secure that benefit was the amount actually received, i.e. making no allowance for the contribution generating any return prior to payment. (If this supposition is correct it is unclear whether the officer

concerned was judging the matter solely with hindsight or whether he was taking the view that this was what the Appellants had agreed at the outset.) The officer must then have taken the view that each of NSP, DWSL and JBL were to be provided the same benefits under the WJL FURBS such that the balance of the *in specie* contribution should be divided equally between them.

133. On the basis that the officer concerned did not know of the £3,000,000 payment to JBL when he issued the closure notices, the allocation that he should have made in the amendments pursuant to his closure notices should presumably have been £2,990,000, £148,000 and £248,000 to each of JBL, VAL and DJM, with the balance of £6,939,000 divided equally between NSP and DWSL (i.e. £3,469,500 each). However the matter is viewed, we do not think that the amendments made pursuant to the closure notice can stand. We therefore reject HMRC's submissions to that effect.

Sham or other pretence

134. We next address HMRC's suggestion that the whole arrangement was some form of sham or other pretence. We have already indicated our difficulty in distinguishing this submission from HMRC's primary and alternative cases (see paragraph 110 above). HMRC do not say the WJL FURBS is a sham: they have accepted that £34,000 was contributed to it and have taxed those sums under section 386. Similarly, we do not think that HMRC say that the payments made to JBL, VAL and DJM were a 'sham' in the sense of being something other than a payment of relevant benefits from the Scheme, for example a payment of ordinary earnings. The same must be the case for the value of the Properties contributed to the WJL FURBS given that the officer's closure notice seeks to tax that the whole value under section 386 as a contribution to the WJL FURBS.

135. The nature of the Appellants' arrangement was that the Company transferred the Properties to the Appellants and ACP as Trustees on the clear 'understanding' that the Trustees would immediately contribute the Properties to the WJL LLP. As such, the 'reality' of the arrangement might be said to be the acquisition by the WJL FURBS of a membership interest in the WJL LLP with the benefit of a capital contribution of £10,325,000 that would provide the basis for it receiving the cash it needed to make payments to JBL, VAL and DJM. In reality, the contribution of the Properties to the WJL FURBS might be said never to have been intended to be "with a view to the provision of relevant benefits" because it was always intended that the Trustees would immediately transfer the Properties to the WJL LLP in exchange for their membership interest in the WJL LLP.

136. Such an analysis would itself raise difficult questions under section 386 as well as questions relating both to the deductibility of the Company's contribution and to the value that the Company should bring into account for what was in reality the extraction of the Properties and their transfer to the WJL LLP. Neither party suggested, however, that we should view matters in this way and from the Appellants' perspective we do not think that they can deny the legal form of the arrangement that they adopted. The Properties were land originally acquired for development by the Company and if the Trustees were to realise their value for the benefit of the WJL FURBS they presumably had to enter into some arrangement to enable the Properties to be developed and then sold. Their contribution of the Properties to the WJL LLP

on 1 April 2006 was their way of achieving that aim and does not deny their initial acquisition of the Properties on 31 March 2006. We therefore see no scope for any argument based on 'sham or other pretence' that characterises the transactions as in some way different from the legal form that they took (and no argument was put on this basis).

Agreement as to the allocation of the in specie contribution

137. We have noted the fact that the Trustees and the Scheme Administrator failed to notify the Appellants of any contributions made on their behalf or to agree their Member's Interest as required by the Trust Deed and Rules. If an amount is in fact contributed for the benefit of a particular employee, the failure of the Company, the Trustees or the Scheme Administrator to record it as such cannot deprive it of its character as a contribution on behalf of that employee: in effect, a scheme member would be entitled to have the matter correctly recorded.

138. This would apply to the cash contributions made on 16 March 2006. The Company's letter of that date would stand as the record of the contributions required by Clause 5 of the Trust Deed. It does not appear, however, that the Trustees agreed with each scheme member which part of those contributions should be applied to secure which benefits, as contemplated by Rules 2[a][iii] and 2[b][ii]. Similarly, ACP as the Scheme Administrator apparently did not provide as required by Rule 13[i] any notification of the nature of the benefit agreed with him in accordance with Rule 2[a][iii]. Their failure to record matters in these respects cannot deny the fact that cash contributions were made on behalf of each of the Appellants.

139. The Appellants say that no record was made in respect of the *in specie* contribution because that contribution was a general contribution to the WJL FURBS and was not made in respect of any particular employee. Certainly, the Company's minute was in terms of securing retirement benefits for scheme members, "both current and future" (see paragraph 13 above). A problem with this, however, is that the Trust Deed and the Scheme Rules appear to contemplate that the Company can only make contributions in respect of "Members", which (as we have noted) only contemplates current Members (see paragraph 42 above). Furthermore, the definition of a Member's Interest is such that a scheme member only becomes entitled to benefits under the Scheme if contributions are in fact made by him or on his behalf.

140. Rule 3 envisages the payment of a pension (see paragraph 49 above) subject to the provisions of Rule 6, which allows a scheme member to elect that part or the whole of his interest be used to provide him with a cash sum benefit. Under Rule 6 the scheme member's election must be exercised by written notice to the Scheme Administrator before retirement. There was no evidence to suggest that any of JBL, VAL or DJM made such an election. Nevertheless, the Trustees resolved to pay them their sums notwithstanding the absence of any written election to that effect. More to the point, the payments could only be made to the extent that the Trustees could attribute the monies or other assets of the Scheme to the contributions that had been paid by them or by the Company on their behalf.

141. Technically, the drafting of the Trust Deed and Rules might permit an argument to the effect that the Trustees could attribute a significantly larger amount of the

Scheme's assets (i.e. derived from an unallocated *in specie* contribution) to the much smaller contributions made on a scheme member's behalf (i.e. the cash contributions) on the basis that the scheme member was entitled to share in a proportionate part of surplus assets held by the Trustees for the purposes of the WJL FURBS. On the other hand, the payments made to JBL, VAL and DJM do not represent a share in the fund assets that is in any way proportionate to the initial cash contributions made on their behalf. The implication must be that part of the *in specie* contribution was in fact a contribution by the Company on their behalf even though the Company refrained from recording it as such.

142. From the Appellants' perspective the 'cost' to the Company of contributing the Properties to the WJL FURBS was £3,236,577 (as per its accounts). This was to fund payments of a broadly similar amount totalling £3,400,000 to JBL, VAL and DJM, while DWSL and NSP were to receive nothing – or, at least, nothing immediately (neither being on the verge of retirement). This might explain why DWSL and NSP were the initial WJL FURBS members: possibly, it was always agreed that they were to receive nothing immediately but the 'split' between JBL, VAL and DJM was still under discussion and DJM in particular wanted to consult his wife on the arrangement (see paragraph 16 above). Given the timing constraints of the planning that required everything to be set up before the end of the current tax year, DWSL and NSP may have set the arrangements in motion while JBL, VAL and DLM were finalising matters between themselves. We think it unnecessary to make any finding to that effect: the main point is that the sum paid by the Company to the WJL FURBS was with a view to the provision of relevant benefits for JBL, VAL and DLM in the amounts that were eventually paid and which we have concluded were agreed at the outset, even if not formally recorded until later.

143. This then accords with the Trust Deed and Scheme Rules notwithstanding that the matter was not formally recorded as that Deed and those Rules envisaged. As we have concluded (see paragraph 53 above), a scheme member only acquires an interest to the extent that contributions are paid by him or by his employer on his behalf. In the present case the Company was contributing the Properties which had a known cost to the Company and a current market value somewhat in excess of that cost, on the basis that previous cash contributions and the Properties (through the medium of the WJL LLP) would fund payments of £3,000,000, £150,000 and £250,000 to each of JBL, VAL and DJM respectively.

144. Given that the Properties were to be immediately contributed to the WJL LLP in return for an equivalent Member's Share in the WJL LLP and that under the LLP Agreement no Member was entitled to interest on his Member's Share, we think it reasonable to assume that the Company's contribution to the WJL FURBS in respect of JBL, VAL and DJM should be taken to be the amount that they eventually received. Those amounts are taxable under section 386 on each of them as sums paid with a view to the provision of relevant benefits for each of them.

Allocation of the residual value of the in specie contribution

145. On the basis that the "sum paid" through the Company's in specie contribution of the Properties to the WJL FURBS is their market value and not their cost to the Company, the agreement that £3,400,000 of that value was contributed to secure the

provision of relevant benefits to three of the Appellants leaves an unallocated balance of value, in respect of which the Company has nevertheless claimed a deduction (albeit in an amount that, we understand, has subsequently been reduced).

146. As it appears, it seems never to have been envisaged that the Company's contribution of the Properties should represent a contribution to the WJL FURBS on behalf of DWSL or NSP. The Company's minute, resolving to set up the FURBS, stated that the *in specie* contribution was being made for current and future scheme members. On that basis nobody would acquire any Member's Interest (and therefore any entitlement to relevant benefits) under the Scheme Rules by reference to the contributed value of the Properties in excess of what was needed to pay the other three Appellants their retirement lump sums. Undoubtedly NSP and DWSL had been admitted as scheme members (and a cash contribution had been paid in respect of each of them) but they could only become entitled to benefits to the extent that they could show that the WJL FURBS assets at the relevant date were attributable to contributions paid by them or on their behalf.

147. Mr Sokol QC suggested in reply that there might perhaps be a resulting trust in favour of the Company, on the basis presumably that this must follow if the Company could not make unallocated contributions to the WJL FURBS. However, the Company plainly intended to contribute the Properties to provide retirement benefits for JBL, VAL and DJM (as we have found). We do not think that in some way it failed to make a valid contribution of the Properties so that balance of any value was not held by the Trustees for the benefit of scheme members. To the extent that the Company might have thought that it was able to contribute any balance of value for the benefit of *future* scheme members, it may not beyond the bounds of argument that the Trustees held that value on a general trust for future scheme members pending their admission and the receipt of contributions by them or on their behalf. However, we think this an unlikely outcome.

148. It was nevertheless the case that each of NSP and DWSL had a Member's Interest as a result of the initial cash contributions and they were the sole scheme members once JBL, VAL and DJM are removed from consideration. It is true that it was not until 10 November 2008 that the Trustees wrote to the Scheme Administrator, ACP, to confirm that no further benefits would be paid to VAL and DJM beyond the payments of £150,000 and £250,000 that they had already received. No equivalent confirmation appears to have been given in respect of JBL. On the other hand, we have concluded that the amount contributed by the Company in respect of each of JBL, VAL and DJM was the amount that all concerned had agreed they would receive as their retirement benefit under the Scheme. That would have exhausted the contributions made on their behalf and therefore the benefits to which they were entitled. Accordingly, we think that no further allocation falls to be made to JBL, VAL and DJM by virtue of section 388. Having regard to "B" and "C" in the formula no further benefits were due to them beyond what they had already secured through the Company's contributions on their behalf.

149. This arrangement devised by (or for) the Appellants would inevitably leave NSP and DWSL in place as the only persons currently entitled to whatever value remained within the WJL FURBS after the payments out to JBL, VAL and DJM. The reference in the Company's minute to "future" scheme members was consistent with the design

of the arrangement to provide JBL, VAL and DJM with their retirement benefits, allowing the Company to claim a deduction for the market value of the Properties and at the same time provide the basis for claiming that no charge arose on any of the Appellants under section 386(1). We have decided on the facts that this expectation was unrealised so far as JBL, VAL and DJM were concerned and we think that the balance of value must therefore have been contributed and held for NSP and DWSL, notwithstanding the terms of the Company's minute.

150. On that basis it seems to us that section 388 operates to apportion the residual value of the Properties to NSP and DWSL because they are the only other scheme members with a Member's Interest and, necessarily, the balance of value accrued for their benefit at the time. Section 388 operates in the case of a sum paid by an employer in accordance with a non-approved retirement benefits scheme and "with a view to the provision of relevant benefits for or in respect of two or more employees". As we noted in paragraph 121 above, the idea that a payment to a non-approved retirement benefits scheme can escape tax through the expedient of not allocating the payment to any particular employee, even though the only employees that can benefit from the payment at the time are easily identified, does not seem especially plausible bearing in mind the Court of Appeal's approach in *Irving*.

151. On the other hand, "B" and "C" in the formula prescribed by section 388 require one to identify the benefits to be provided in respect of each employee and in the current case this presents some difficulty if in fact the Company did not contribute the excess value of the Properties on behalf of either NSP or DWSL. If that is the case, however, it would tend to suggest that the excess value disappeared into some form of 'limbo': benefits depend upon monies and assets held by the WJL FURBS being attributed at the appropriate time to contributions paid by a scheme member or by his employer on his behalf. If the excess value cannot be attributed to some scheme member by virtue of his allocated contributions, it will never be applied in the provision of benefits.

152. We have however concluded that the excess value must be taken to represent a sum paid with a view to the provision of relevant benefits for or in respect of NSP and DWSL, as the only remaining scheme members each of whom is entitled to a Member's Interest either because that value was in fact contributed by the Company for their benefit or because, in any event, the Company's previous cash contribution provided them with such an interest. It seems to us that the benefits that they secured at the time were those represented by the excess value contributed and that as they had the same entitlement overall, the excess value should be divided between them equally. After allowing for the amount contributed in respect of JBL, VAL and DJM, the remaining value at 31 March 2006 is £6,925,000 or £3,462,500 each. To the extent that neither of them has or is ever likely to receive any benefit from the WJL FURBS in respect of that value, we assume that there will be the scope for them to obtain relief under section 392.

Claims for relief under section 392

153. Both NSP and DWSL had claimed relief under section 392 on the basis that if they were liable to tax under section 386 in respect of the Company's *in specie* contribution of the Properties they were nevertheless entitled to relief on the basis that

no payment in respect of or in substitution for the benefits secured by the contribution had been or would ever be made.

154. Section 392 allows an application for relief in those circumstances but relief is only given "if an officer of Revenue and Customs is satisfied that the conditions in subsection (1) are met". Mr Sokol QC on behalf of NSP and DWSL contended that we could nevertheless give effect to the claim for relief on the basis that our jurisdiction permitted us to determine the self-assessments in respect of each of them and that we could readily see that the WJL FURBS had become insolvent and had been dissolved. There was therefore no prospect of NSP or DWSL receiving any amount in respect of whatever benefits the WJL FURBS had originally promised them.

155. We do not think that we were given a clear enough account of how the WJL FURBS' capital account with the WJL LLP had been dealt with, and how it was that a deficit arose leading to its expulsion from membership (see paragraph 77 above), to determine this matter. In any event, Mr Rivett for HMRC resisted this suggestion on the basis that relief under section 392 was only available in circumstances in which an officer was satisfied that it was available and that it did not confer any jurisdiction on the Tribunal to determine the matter. Nor, indeed, did section 392 confer any right of appeal to the Tribunal if the officer was not satisfied, although in the present case the relevant officer had in fact reached no decision as to whether relief under the section should be granted.

156. In relation to this aspect of the matter we no longer have to consider the matter in detail because it has been resolved for us by the Upper Tribunal in *HMRC v Mitesh Dhanak* [2014] UKUT 68 (TCC) (in which HMRC were also represented by Mr Rivett). In a detailed consideration of the issues Mr Justice David Richards concluded that there was no appeal to the Tribunal from a refusal of an application for relief. Accordingly, Mr Dhanak's attempted appeal to this Tribunal from such a refusal was struck out.

157. Furthermore, the Judge also concluded in *Dhanak* that even if he had held that a refusal of an application for relief under section 392 could be challenged in the context of a statutory appeal against amendments made by a closure notice, he would have held that it was not open to Mr Dhanak to do so in the circumstances of his case. This was because the closure notices had been issued before the event that was said to give rise to the claim for relief. As the Judge put the point at [61]—

> "However widely one identifies the subject matter of the enquiries and closure notices, they cannot in my judgment include an application for relief under section 392 which had not been made by the time of the closure notices, based on events which did not occur until some 8 months after the closure notices."

The same is true for both NSP and DWSL.

Decision

158. Accordingly we would determine these appeals as follows—

(1) We dismiss NSP's appeal and would increase his taxable income from £3,309,666 to £3,462,500 (being his 50 per cent share of the balance of value contributed to the WJL FURBS after allowing for the value contributed on behalf of JBL, VAL and DJM);

(2) We dismiss DWSL's appeal and would increase his taxable income from £3,309,666 to £3,462,500 on the same basis as NSP;

(3) We would allow JBL's appeal to the extent that we would reduce the increase in his taxable income to £3,000,000 from £3,309,666;

(4) We dismiss DJM's appeal;

(5) We dismiss VAL's appeal.

159. As we believe that there may remain an issue concerning the correct value of the Properties at the time they were contributed and we understand that we were only asked to reach a decision in principle, we do not finally determine the appeals in the above amounts pending the final determination of that value. Based on our findings, however, this should now only be a matter of concern to NSP and DWSL. To the extent that it is necessary for us to determine the appeals finally the parties are at liberty to apply for us to do so.

160. Mr Sokol QC included detailed written submissions seeking indemnity costs in the event that he should be successful. We see no basis for this. To the extent that either party considers that it is entitled to costs as a result of our decision that party make apply in the usual way pursuant to this Tribunal's rules.

161. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

MALCOLM GAMMIE
TRIBUNAL JUDGE

RELEASE DATE: 29 August 2014