



Appeal number: UT/2016/0040

INCOME TAX – registered pension scheme – scheme funds invested at member’s direction in preference shares of finance company - finance company lending its assets to third party lender who made loan to scheme member - scheme member obliged as condition of receiving loan to ensure scheme assets remain invested in finance company preference shares - whether loan to scheme member was unauthorised member payment - whether payment made in connection with the investment in the preference shares - ss 161 (3) and (4) Finance Act 2004

**UPPER TRIBUNAL
TAX AND CHANCERY CHAMBER**

MARK DANVERS

Appellant

- and -

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

**TRIBUNAL: The Hon. Mrs Justice Rose DBE
 Chamber President
 Judge Timothy Herrington**

**Sitting in public at The Rolls Building, Fetter Lane, London EC4 on 16
November 2016**

Frances Ratcliffe, Counsel, for the Appellant

**Laura Poots, Counsel, instructed by the General Counsel and Solicitor to HM
Revenue and Customs, for the Respondents**

DECISION

Introduction

1. Mark Danvers (“Mr Danvers”) appeals against a decision by the First-tier Tribunal (“FTT”) (Judge Poole and Ms Janet Wilkins CTA) released on 5 January 2016 (“the Decision”). The FTT dismissed Mr Danvers’ appeal against an amendment to his tax return for the year 2009/2010. The amendment imposed an additional tax charge of £10,260.80 on Mr Danvers by way of an unauthorised payment charge and unauthorised payment surcharge under the provisions of the Finance Act 2004 (“FA 2004”) concerning registered pension schemes.

2. The FTT found that a loan of £18,656.69 (“the Loan”) by a lending company G Loans Limited (“G Loans”) to Mr Danvers fell within s 161(3) and (4) FA 2004 as being made in connection with an investment made by Mr Danvers’ self-invested pension scheme, the HD SIPP. The relevant investment was that made by the HD SIPP in a finance company, KJK Investments Limited (“KJK”), in circumstances where it was a condition of the making of the Loan that the HD SIPP invest the whole of its net assets in cumulative preference shares of KJK and where G Loans was funded substantially by loans made to it by KJK.

3. The FTT found that the investment made by the HD SIPP in the KJK preference shares had the necessary connection with the Loan because on the facts the investment and the Loan were inextricably linked.

4. Consequently, the FTT concluded that the Loan was an unauthorised payment for the purposes of FA 2004 and accordingly Mr Danvers was properly subject to an unauthorised payments charge pursuant to s 208 FA 2004 and an unauthorised payments surcharge pursuant to s 209 FA 2004.

5. Permission to appeal against these findings was given by Judge Poole on 3 March 2016. We were told that this was originally a lead case with some 80 other appeals remaining stayed pending the outcome of this case notwithstanding the revocation of the rule 18 order.

The Facts

6. The FTT made its findings of fact at [4] to [26] of the Decision. The FTT heard no oral evidence, and therefore its findings rely to a significant extent on the documentary evidence that was before it. The FTT’s findings can be summarised as follows.

7. Mr Danvers was at the time of the relevant events 41 years old. He was therefore below the statutory age at which he was entitled to take benefits from his pension fund without incurring the income tax charge that is designed to deter such access.

8. In mid-November 2009 Mr Danvers decided to transfer his existing pension funds with Windsor Life and Winterthur Life, which at that time had a value of

approximately £35,000, to the HD SIPP, a registered pension scheme. The FTT found that this decision was taken specifically with a view to the obtaining of a loan.

9. The FTT referred to two documents which it found Mr Danvers had seen before he reached his decision to transfer his pension funds.

5 10. The first of these documents was headed “G Loans Questions and Answers”. It described a “G Loan” as “a loan whereby the capital is repaid using the proceeds from your personal pension fund”. This document referred to the fact that a participant’s pension fund had to be invested with “a company on an approved panel” in order to
10 “ensure that G Loans Ltd can be as sure as possible that sufficient funds will be available to repay your loan.”

11. The second of these documents was a document headed “KJK Investments Limited – Information Memorandum”, which gave details of a proposed issue of cumulative preference shares by KJK. The FTT found that this document was issued sometime shortly before 1 May 2009. The proposed business of KJK was said in this
15 information memorandum to be “taking advantage of the current difficulties in the lending market” by specialising in “wholesale lending, i.e. lending to other lenders”. Typical opportunities were said to include lending to bridging finance companies and lending to other companies offering unsecured loans (with which KJK was said to “have connections”). It was said that those other companies would then use the
20 money, among other things, to advance loans where the client can provide evidence that he will be getting monies in the future to repay the loan, and included as an example the drawing of a pension.

12. We note that a “snapshot” of KJK’s activities as at 30 June 2013 showed that 58.8% of KJK’s outstanding loan book, a sum of £6,968,221, was represented by
25 lending to G Loans. The abbreviated accounts of G Loans for the year ended 31 January 2013 showed debtors of £7,006,884 and long-term creditors of £6,830,115. Although the FTT found there was no direct evidence before it beyond the trading statement of KJK as to where G Loans obtained its finance, it appears that most, if not all, of G Loans’ funding came from KJK.

30 13. On 25 November 2009 Mr Danvers signed three documents as follows. First, he signed an application to become a member of the HD SIPP and to be a co-trustee of his fund held within it. Second, he signed a form indicating that he was acting on an “execution only” basis and not seeking any advice from the HD SIPP. Third, he signed an instruction to the trustee of the HD SIPP to invest £34,899 in KJK
35 cumulative preference shares. The FTT found that Mr Danvers expected the investment of funds in KJK to generate the loan from G Loans to him. The FTT made no findings as to whether Mr Danvers believed that KJK would lend funds (directly or indirectly) to G Loans to finance the loan to him but stated that its decision would be the same whether or not that was the case.

40 14. The preference shares issued by KJK carried a cumulative dividend at the rate of 6% per annum and were redeemable at the option of the holders by giving 3

months' notice to KJK at any time after 1 January 2014; they were also redeemable at the option of KJK by giving 3 months' notice at any time after 1 January 2015.

15. Mr Danvers became a member of the HD SIPP on 1 December 2009. Transfer payments to this scheme were made from Mr Danvers's existing pension providers on 3 and 8 December 2009. The total of the sums transferred was £35,447.72.

16. On 11 December 2009, Mr Danvers signed a loan agreement with G Loans under which G Loans agreed to lend him the amount of the Loan. G Loans signed this agreement on 16 December 2009. The FTT found these to be the key terms of the Loan:

- 10 (1) it was advanced "on an interest only basis and the capital will be repaid from the proceeds of your pension fund";
- (2) interest was payable at the rate of 5.5% for the first year (which was to be paid in advance) and thereafter at "5% above bank base rate", due annually in arrears;
- 15 (3) the appellant was required to pay an initial fee of 5% of the amount of the Loan (£932.83);
- (4) the "maximum amount the borrower will be required to repay" was fixed at "the amount received, net of tax, from the borrower's pension fund" (another condition in the agreement provided that "the borrower will not have to repay more than the tax free cash and the net income that he receives from his pension");
- 20 (5) the "method of repayment" was identified as "From the net proceeds of the borrower's pension";
- (6) it was provided that "the borrower will utilise his tax free cash to reduce the loan balance. If the tax free cash is not sufficient to repay the entire loan, the borrower will utilise any net income drawn from the pension benefits";
- 25 (7) if the appellant died then the Loan would become immediately repayable, with interest, but the maximum amount to be repaid on death would be "the net death benefits from the borrower's pension";
- 30 (8) it was stated that "this loan has been granted due to the fact that the borrower has a total of approximately £35,000 invested in personal pensions with Windsor Life and Winterthur Life", and that "as a condition of the loan being granted, the pension must be transferred within 4 weeks (if not already) of receiving the loan to a Self Invested Pension Plan (SIPP) with HD SIPP and after HD SIPP's fees are paid the remaining monies must be used to buy ordinary shares and cumulative preference shares in KJK Investments Limited";
- 35

(9) it was provided that KJK would be liable for any fees subsequently due to HD SIPP, and that if it failed to pay any such fees in respect of the appellant's SIPP, "the loan agreement becomes unenforceable";

5 (10) it was provided that "the borrower cannot disinvest monies from KJK Investments Ltd or transfer monies away from the HD SIPP without the written permission of G Loans Ltd. or unless the loan is repaid in full. If any dividends or other monies are paid from KJK Investments Ltd into the borrower's SIPP account the lender can insist on where these monies are subsequently invested unless the loan is repaid in full";

10 (11) it was provided that "if any of the above conditions are not met, the loan will become due to be repaid immediately and interest will immediately accrue at the default rate of 24% per annum".

15 17. On 16 December 2009 Mr Danvers received £16,753.71 from G Loans, being the amount of the agreed loan after deduction of a fee of 5% of the loan amount and the first year's interest in advance.

18. On 17 December 2009, pursuant to the authority given by Mr Danvers on 25 November 2009, the HD SIPP applied for and was allotted 34,899 £1 preference shares in KJK fully paid up at par.

20 19. We were told and should record that both KJK and G Loans are now in liquidation.

The Law

25 20. As stated in s 149 FA 2004, Part 4 of that Act (comprising sections 149 to 284) contains tax provision about pension schemes. In particular, Chapter 2 of that Part is about the registration and deregistration of pension schemes, Chapter 3 is about the payments that may be made by registered pension schemes and related matters, Chapter 4 deals with tax reliefs and exemptions in connection with registered pension schemes, Chapter 5 imposes tax charges in connection with registered pension schemes and Chapter 7 makes provision about compliance.

21. Section 150 (1) FA 2004 defines "pension scheme" as follows:

30 "(1) In this Part "pension scheme" means a scheme or other arrangements, comprised in one or more instruments or agreements, having or capable of having effect so as to provide benefits to or in respect of persons-

- (a) on retirement,
- (b) on death,
- 35 (c) on having reached a particular age,
- (d) on the onset of serious ill-health or incapacity, or
- (e) in similar circumstances."

22. A pension scheme which meets the requirements for registration under Chapter 2 of Part 4 FA 2004 and is duly registered under those provisions is, pursuant to s 150 (2) FA 2004 a “registered pension scheme”. The HD SIPP met the requirements for registration pursuant to s 153 FA 2004 and accordingly is a registered pension
5 scheme. In the course of her submissions on behalf of Mr Danvers, Ms Ratcliffe emphasised that the HD SIPP in this case had been registered by HMRC suggesting that this conferred some legitimacy on the overall arrangements. We do not see that the fact that HD SIPP was a registered scheme, or that the arrangements were not a sham, is relevant to the issues before us. It is clear from the provisions we describe in
10 the following paragraphs that the charges which are the subject of this appeal apply to payments from registered pension schemes.

23. As a consequence of being registered, the scheme is subject to the restrictions on payments out of the scheme contained in Chapter 3 of Part 4 FA 2004 (breach of which can result in tax charges being levied pursuant to Chapter 5 of Part 4 FA 2004)
15 but the scheme and its members benefit from the tax reliefs and exemptions set out in Chapter 4 of Part 4 FA 2004.

24. Chapter 3 of Part 4 FA 2004 is headed “Payments by Registered Pension Schemes”.

25. The concept of *a payment by* a registered pension scheme is the subject of elaboration in the legislation in two important respects. First, the meaning of the
20 word “payment” is set out in section 161 FA 2004. This provides (so far as relevant):

“(2) “Payment” includes a transfer of assets and any other transfer of money's worth.

(3) Subsection (4) applies to a payment made or benefit provided under or in
25 connection with an investment (including an insurance contract or annuity) acquired using sums or assets held for the purposes of a registered pension scheme.

(4) The payment or benefit is to be treated as made or provided from sums or
30 assets held for the purposes of the pension scheme, even if the pension scheme has been wound up since the investment was acquired

....

(8) For the purposes of this section whether a person is connected with another person is determined in accordance with section 993 of ITA 2007.”

26. Secondly, as to when a payment is regarded as having been made ‘by’ a
35 registered pension scheme, section 279(2) FA 2004 provides that:

“(2) In this Part references to payments made, or benefits provided, by a pension scheme are to payments made or benefits provided from sums or assets held for the purposes of the pension scheme.”

27. Section 160 FA 2004 then imposes restrictions on what payments can and cannot be made legitimately by a registered pension scheme. Section 160(1) provides that:

5 “(1) The only payments which a registered pension scheme is authorised to make to or in respect of a person who is or has been a member of the pension scheme are those specified in section 164.”

28. Thus an unauthorised member payment is defined in section 160(2) as:

10 “(a) a payment by a registered pension scheme to or in respect of a person who is or has been a member of the pension scheme which is not authorised by section 164, and

(b) anything which is to be treated as an unauthorised payment to or in respect of a person who is or has been a member of the pension scheme under this Part.”

29. Authorised member payments are set out in section 164(1) FA 2004 which provides that:

15 “The only payments a registered pension scheme is authorised to make to or in respect of a person who is or has been a member of the pension scheme are—

(a) pensions permitted by the pension rules or the pension death benefit rules to be paid to or in respect of a member (see sections 165 and 167),

20 (b) lump sums permitted by the lump sum rule or the lump sum death benefit rule to be paid to or in respect of a member (see sections 166 and 168),

(c) recognised transfers (see section 169),

(d) scheme administration member payments (see section 171),

(e) payments pursuant to a pension sharing order or provision, and

25 (f) payments of a description prescribed by regulations made by the Board of Inland Revenue.”

30. The ‘scheme administration member payments’ referred to in subsection (d) there are those set out in section 171 FA 2004 which provides as follows:

30 “(1) A “scheme administration member payment” is a payment by a registered pension scheme to or in respect of a person who is or has been a member of the pension scheme which is made for the purposes of the administration or management of the pension scheme.

(2) But if a payment falling within subsection (1) exceeds the amount which might be expected to be paid to a person who was at arm's length, the excess is not a scheme administration member payment.

35 (3) Scheme administration member payments include in particular—

(a) the payment of wages, salaries or fees to persons engaged in administering the pension scheme, and

(b) payments made for the purchase of assets to be held for the purposes of the pension scheme.

5 (4) A loan to or in respect of a person who is or has been a member of the pension scheme is not a scheme administration member payment.”

31. It was common ground that the payment made when HD SIPP bought the shares in KJK was a scheme administration member payment within section 171(3)(b).

32. It was also common ground that Part 4 FA 2004 should be interpreted and
10 applied in accordance with the purposive approach set out by the House of Lords in *Barclays Mercantile Business Finance Limited v Mawson* [2004] UKHL 51, [2005] STC 1. The two steps which are necessary in the application of any statutory provision are first, to decide, on a purposive construction, exactly what transaction will answer to the statutory description and secondly, to decide whether the
15 transaction in question does so. Ms Ratcliffe also reminded us of the cardinal principle that a person is entitled to organise his or her affairs so that the minimum amount of tax is paid; whether they achieve their aim is a question to be determined by applying the statute interpreted purposively to the facts found realistically.

33. In following this purposive approach, we should therefore have regard to the
20 purpose of the provisions relating to unauthorised payments. In *Willey v HMRC* [2013] UKFTT 328 (TC) the FTT (Judge Cannan) provided a helpful summary of the purpose behind the various tax charges which can arise under Chapter 5 of Part 4 FA 2004 at [6] as follows:

25 “FA 2004 contains a prescriptive regime in relation to the payments that registered pension schemes are authorised to make and the consequences of unauthorised payments. The rationale is to ensure that the tax reliefs and exemptions in respect of contributions to registered pension schemes are available only to the extent that the pension schemes genuinely make provision for the benefit of members on retirement, subject to various statutory limits. The
30 compliance regime and reporting requirements set out in FA 2004 are directed towards the same end.”

34. Therefore, should there be an unauthorised member payment, such as one that is made before the scheme member concerned reaches his retirement date, then the taxes imposed as a result of that unauthorised member payment will in effect clawback tax
35 reliefs and exemptions that have previously been given, the policy being that those reliefs and exemptions are only available in so far as benefits from the pension scheme are taken on retirement. In this case therefore, we need to determine whether, construing the provisions regarding unauthorised payments purposively, those provisions were intended to apply to the Loan, viewed realistically.

40 35. It is also common ground that the Explanatory Notes to the Finance Bill 2004 can be relied upon as an aid to construction and we refer to the relevant Notes later.

The Decision

36. The FTT identified the issue to be determined on the appeal as being whether the Loan was made “in connection with an investment ... acquired using” the assets of the HD SIPP within the meaning of section 161(3). It then drew the following conclusions at [59] from the facts that it had found at [4] to [25] of the Decision:

“It is apparent from the facts set out above that the investment by the HD SIPP in the KJK preference shares was inextricably linked to the loan made to the appellant. We accept that KJK used the money received from its issue of preference shares (including the issue made to HD SIPP in respect of the appellant’s fund) for its purposes generally and did not specifically allocate the money received from any particular investor for lending to any particular borrower; nonetheless it is quite clear that the entire arrangement was orchestrated from beginning to end to ensure that the appellant received his expected loan as a result of transferring his pension funds to the HD SIPP and instructing it to invest them in the KJK preference shares. In the absence of fraud (i.e. the theft of the appellant’s pension funds) there was in our view never any realistic likelihood that the transfer of his pension funds to the HD SIPP would not result in those funds being invested in the KJK preference shares and the appellant receiving a loan of an agreed amount from G Loans. That, we find, was certainly the appellant’s expectation.”

37. At [60] the FTT quoted with approval the passage from *Willey* set out at [33] above as demonstrating “the purpose of the various tax charges”.

38. At [61] the FTT distinguished the arrangements in this case with a loan being advanced to a pension scheme member on the basis that he or she is expected to repay that loan out of an anticipated tax-free cash lump sum arising under the pension arrangements. The FTT said that there were extra features in this case, namely the requirement to transfer the borrower’s pension fund into a new scheme and authorise investment of that fund in specified investments as a condition of accessing the loan. Neither did the FTT consider it to be relevant that Mr Danvers continued to have his rights in his pension fund under the rules of the HD SIPP because the unauthorised payment charge was not levied by reference to any change in value of the underlying fund as a result of an unauthorised payment but by reference to the amount of the payment: see [62] of the Decision.

39. The FTT declined to reach its conclusion by considering whether the arrangements were an “abuse” of the registered pension scheme reliefs, finding that the better approach was simply to interpret the words used by Parliament in their context, applied to the facts of the case: see [63] of the Decision.

40. It then concluded at [64]:

“ In the circumstances outlined above in this decision, in particular given that:

(1) the appellant transferred his pension funds to HD SIPP with a specific instruction to invest those funds in preference shares of KJK; and

(2) he did so specifically in order to obtain the Loan from G Loans,

we have no hesitation in finding that the loan to the appellant was made “in connection with” the KJK preference shares, an investment acquired using sums held for the purposes of a registered pension scheme”

5 **Grounds of Appeal and issues to be determined**

41. On 3 March 2016 Judge Poole granted permission to appeal on the following two grounds:

10 (1) the FTT erred in law in finding that on a correct construction of s 161 (3) and (4) FA 2004 the Loan was made “in connection with” the investment by the HD SIPP because:

(a) it failed to give due regard to the purpose of the legislation when construing the scope and intention of those provisions;

15 (b) the purpose of those provisions is to prevent payments from a registered pension scheme or from an investment held for the purposes of the pension scheme, to or in respect of members of that scheme or persons connected with a person who is or has been a member of the scheme in question;

20 (c) in turn, this is to ensure that pension scheme assets are not used other than for the benefit of members in the provision of pension benefits to or in respect of those members;

25 (d) the purpose of those provisions is not to prevent legitimate commercial arrangements between registered pension schemes and third parties (namely those not comprising members of the pension scheme or persons connected with a member of the pension scheme) nor is it to prevent legitimate commercial arrangements between those who happen to be members of registered pension schemes and entities unconnected with the pension scheme in question; and

(2) the FTT erred in law in finding that the investment by the HD SIPP in the KJK preference shares was inextricably linked to the Loan when:

30 (a) the Loan was a commercial loan between a lender and a borrower, the lender being wholly unconnected with the HD SIPP;

(b) that the borrower was a member of a SIPP did not render the Loan inextricably linked to the pension scheme investment;

35 (c) there was no requirement that the Loan be repaid from Mr Danvers’s pension with the HD SIPP;

(d) the Loan was made in advance of the HD SIPP’s investment in KJK: the funds loaned did not emanate from the investment in KJK; and

(e) KJK's business involved lending to a number of companies as well as G Loans hence it was not the case that the monies invested in KJK on behalf Mr Danvers were leading directly to G Loans in any event.

42. We should add for completeness that Mr Danvers disputed before the FTT whether a loan could amount to a payment at all within Part 4 of FA 2004. This point was determined against Mr Danvers by the FTT and was not made the subject of his application for permission to appeal.

43. In summary, therefore, the issues we have to determine are:

(1) what is the correct construction of s 161(3) and (4) FA 2004 as regards when a payment is properly to be treated as having been made from sums held for the purposes of the pension scheme because that payment is **made under or in connection with** an investment acquired using sums held for those purposes ('Ground 1')?

(2) applying the provisions, properly construed, to the facts of this case, was the Loan payment to be treated as having been made from sums held for the purposes of the pension scheme because the Loan monies were paid by G Loans 'under or in connection with' the investment comprising KJK shares which had been acquired using sums from HD SIPP ('Ground 2')?

Discussion

44. We shall deal with each of the two grounds summarised at [43] above in turn as follows.

Ground 1: the proper construction of section 161(3) and (4)

45. Ms Ratcliffe submitted that s 161(3) and (4) FA 2004, which treat a payment as having been made by a pension scheme if it is made "under or in connection with" an investment which is acquired using pension scheme sums or assets, only catches payments where there is a direct connection between a pension scheme investment and the payment made to the member, not where the connection is indirect. In effect, Ms Ratcliffe says that "in connection with" should be read as "from" or "by" so that the provision is confined to a payment to a member directly sourced from an investment made by the pension scheme.

46. Ms Ratcliffe submits that in giving these provisions a purposive interpretation it is important to bear in mind that the primary mischief to which Part 4 FA 2004 is addressed is unauthorised payments from a registered pension scheme to or from sums or assets held by the scheme. This is to ensure that pension schemes genuinely make provision for their members on retirement and are not abused for ulterior purposes. The regime in Part 4 FA 2004 is designed to tax those individuals who seek to use their registered pension schemes other than for the purposes of providing retirement benefits. It is not intended to thwart proper savings and investment in schemes whose purposes are to provide such benefits.

47. In support of her analysis of the legislation Ms Ratcliffe relies on HMRC's Pension Tax Manual; PTM 02600 states as follows:

5 "The legislation treats payments made (or benefits provided) under or in connection with any annuity or insurance contract (or other investment vehicle) purchased using sums or assets held by a registered pension scheme, as payments under the originating scheme.

10 Where the purchased item (annuity, insurance contract, investment vehicle etc.) remains in the ownership of the scheme, then the payment is already considered a payment under the registered pension scheme under section 161(2) Finance Act 2004.

15 Section 161(3) and (4) Finance Act 2004 come to the fore when the scheme does not own the purchased item. Typically, this may arise where a scheme buys an annuity policy from an insurance company 'in the member's name'. Here, the member owns the policy (rather than the scheme) and the insurance company is directly liable to the member.

20 So, for example, where a lifetime annuity is purchased from a money purchase arrangement any payment made by that contract on the death of the annuitant should comply with the authorised pension death benefit rules and lump sum death benefit rule (see PTM070000). If the contract provides an unauthorised member payment the payment will be taxed accordingly (see PTM134000)."

25 48. Ms Ratcliffe also points out that the definition in section 171 FA 2004 of "scheme administration member payments" (that being a kind of authorised payment) permits payment to be made for the purchase of assets to be held for the purposes of the pension scheme (s 171(3) (b) FA 2004) but makes it clear in s171(4) that a loan to or in respect of a person who is a member of the pension scheme is not a scheme administration member payment.

30 49. Ms Ratcliffe therefore accepts that a loan made directly out of the scheme would, by virtue of s 171(4) FA 2004, be an unauthorised member payment. Further she accepts that a loan made to Mr Danvers directly by KJK would also be an unauthorised member payment because it would be a payment made directly from an investment acquired using sums held for the purposes of the registered scheme and would therefore be regarded as 'made ... in connection with' that investment. However, she submits that a loan made by a third party lender, in this case G Loans, would not be caught by s 161(3) and (4) FA 2004 because there was only an indirect connection with an investment in the scheme. In her submission that connection was too remote, on the proper construction of the statutory provisions.

50. We reject these submissions for the following reasons.

40 51. In our judgment, it is clear from the language of the relevant provisions of Part 4 FA 2004 that it is intended that their scope goes wider merely catching payments made "from" investments acquired for the scheme.

52. Had the provisions been intended only to catch payments made “from” investments made with the assets of the scheme then the draftsman could quite easily have said so by using the word “from” rather than “in connection with” in s 161(3). If the draftsman had done so, however, then the word “under” used in the same provision would have been superfluous. This indicates that there was a deliberate choice to use a term with wider meaning and the term “in connection with” was intended to be capable of catching payments that went wider than those which were simply made from an investment purchased with the funds of the scheme, such as a dividend or other distribution, or by the company in which the scheme had made such an investment, such as a loan made by such company to a member of the scheme. It is therefore clear that the legislation does envisage that payments made to a member of a pension scheme by a third party in circumstances where there is a connection between that payment and an investment in the scheme can fall within the scope of the legislation. The statutory provisions should not be construed by substituting different words from those used in the provision itself.

53. We accept that the purpose behind the provisions in Part 4 FA 2004 is to ensure that pension schemes genuinely make provision for the members on retirement and are not abused for ulterior purposes. Clearly, the example given by HMRC in its Pension Tax Manual, quoted at [47] above, of a payment made to a member on his death under an annuity which did not comply with the death benefit rules may properly be regarded as falling within the scope of the provisions. Likewise, a loan made by a company in which the pension scheme had invested, particularly where it was a condition of the loan that the pension scheme would make that investment, would be caught by the provisions and Ms Ratcliffe did not seek to argue otherwise.

54. In using the phrase “in connection with”, s 161(3) FA 2004 gives a clear indication that a connection or link between the payment that the member of the scheme receives and a specific investment which the pension scheme has made must exist in order for the payment to be treated as being one made from the investment itself. The question for us is whether the phrase “in connection with” catches payments where the connection between the investment and the loan goes wider than those examples and, if so, how close the connection needs to be. In our view, the example given by HMRC in the Pension Tax Manual is just but one example of the type of payment that can be caught by the provision. It is a situation well removed from the circumstances that we are considering in this case and gives no indication in itself that the provisions were not intended to catch third-party payments.

55. Ms Ratcliffe seeks to derive support from the wording of s 279(2) FA 2004 which interprets the phrase “payments made, or benefits **provided, by** a pension scheme” as used in Part 4 FA 2004 as meaning “payments made or benefits **provided from** sums or assets held for the purposes of the pension scheme” (emphasis added).

56. Section 279(2) FA 2004 has the limited purpose of making it clear what is meant in the other provisions of Part 4 by “payments made by a registered pension scheme”, a provision which is necessary because the scheme itself will not be a legal person. Whilst the provision uses the phrase “from sums or assets held for the purposes of the pension scheme”, that provision must be construed in accordance with

the extended meaning provided by s 161(4) which provides that a payment is to be “treated as made or provided from sums or assets held for the purposes the pension scheme” where, as provided by s 161(3), it is made “in connection with an investment acquired using sums or assets held for the purposes of the pension scheme”.

5 57. Consequently, the use of the word “from” in s 279(2) does not indicate that it was intended that “in connection with” should be synonymous with “from” in s 161(3). On the contrary, reading the provisions together gives a clear indication that the phrase “in connection with” was intended to bear a wider meaning than “from”.

10 58. Ms Ratcliffe submits that the narrow interpretation she contends for accords with the Explanatory Notes to the Finance Bill 2004 in which it is stated: (emphasis added)

“Briefly the definition of payment ensures that:

- Payments of both money and money’s worth (for example, the transfer of assets) are included;
- 15 • Any payment from the assets of a registered pension scheme, or **from investments acquired using scheme assets**, are included, even if the scheme has since been wound up;
- ...
- 20 • Payments made to persons connected with the member or a sponsoring employer are treated as made for the benefit of the member.”

25 59. In our judgment, the Explanatory Notes to the Finance Bill 2004 do not assist Ms Ratcliffe either. Again, the explanation that the purpose of the provision was to catch any payment “from” an investment acquired using scheme assets cannot be said to be exhaustive of the scope of the provision.

30 60. Miss Poots drew our attention to a further Explanatory Note to the clauses in the Finance Bill 2004 which ultimately became ss 208 and 209 FA 2004. That Note states that those charges were “intended to prevent abuse by the scheme administrator, any member or any employer sponsoring the scheme of the benefits obtained from the tax relief provided to such schemes.” The Note makes it clear that the charges will be imposed on any scheme member who receives a payment or benefit that is not authorised by what was to become Part 4 FA 2004. There is no indication from this Note that the provisions were to be narrowly construed. Indeed, the legislation appears to envisage that this purpose cannot be achieved simply by preventing assets
35 from leaving pension schemes before retirement age.

40 61. Consequently, charges can be imposed in a variety of situations where pension scheme assets are not themselves dissipated, such as a loan from the pension scheme. As Miss Poots submitted, the approach of Part 4 is to give a wide definition to the concept of payment, using broad language, and to then allow benefits to members only in specified circumstances, using the deliberately prescriptive list of authorised payments set out in s 164 FA 2004. That approach is clear from section 160(1) FA 2004 with its emphasis on the “only payments” which a registered pension scheme is authorised to make for the benefit of members of the scheme being those specifically authorised by s 164. With such a rigid prescription of what amounts to an authorised

payment, it is not surprising that the provisions are backed up by widely drawn anti-avoidance provisions with the deterrence of the imposition of income tax charges and surcharges in the event that unauthorised payments are made.

5 62. Ms Ratcliffe drew our attention to a similar provision in s 401 of the Income Tax (Earnings and Pensions) Act 2003 (“ITEPA”) which applies to “payments and other benefits which are received directly or indirectly in consideration or in consequence of, or otherwise in connection with... the termination of a person’s employment...”. As the Upper Tribunal found in *Moorthy v HMRC* [2016] UKUT 13 TCC, in following an earlier Upper Tribunal decision on the predecessor legislation to 10 these provisions, the statutory language was broadly drawn. That can be seen from the use of the words “indirectly” and “otherwise in connection with”, “otherwise” simply meaning “in any way”, consistent with the Parliamentary intention to catch a wide range of payments. Ms Ratcliffe submits that s 161(3) and (4) FA 2004 are not expressed in such broad terms and should not be construed as such.

15 63. We accept that s 401 ITEPA is drafted in wider terms than s 161(3) and (4) FA 2004 and therefore if similar language had been used in the latter provisions then it would catch a wider range of payments. So for example, such language may give rise to some of the concerns that Ms Ratcliffe suggested would exist if a very broad interpretation is adopted, such as pension mortgages, which we deal with below.

20 64. However, in our view the words “in connection with” are also broad in scope. As we have said above, the question is whether there is a link between a specific investment made by the scheme and a payment received by a member of the scheme. In our view the wording is consistent with it being necessary that there is a causal link between the investment and the payment.

25 65. An obvious situation where the necessary link would exist would be if a third party lender was funded entirely by a company in which a pension scheme was invested, loans being made by the investee company to the third party lender only in 30 circumstances where the scheme member was to take up a loan from the third party lender, the amount being lent by the investee company being identical to the amount on-lent to the scheme member. In such a case, the investee company would be a mere conduit for the making of loans from the scheme to the member and would in our view quite clearly come within the anti-avoidance provisions of s 161 (3) and (4) FA 2004.

35 66. However, in our view, the connection can go further than that and would cover an arrangement whereby a scheme member receives a loan from a third party lender and it is a condition of him receiving such a loan that he directs the pension scheme to invest in a particular investment and remain invested in that investment until the loan is repaid. In our view that gives rise to a sufficient causal link between the payment to the member under the loan and the investment made by the pension scheme.

40 67. Viewed realistically, the anti-avoidance provisions are wide enough to bring such a payment within their scope. Despite the scheme’s assets remaining intact, the scheme member has received a benefit from the scheme prior to his normal retirement

date. In our view, we see no difference between this and a direct loan made from the scheme to the member where it is also the case that the investments in the scheme remain intact; in that situation it is simply the case that one of the scheme assets is now represented by a debt owed by the member to the scheme.

5 68. We now deal with Ms Ratcliffe’s alternative argument on the construction of s
161(3) and (4) FA 2004 namely that they are concerned solely with connections
between “connected persons”. Ms Ratcliffe submits it is apparent from s 161(8) FA
2004 that the provisions apply where a payment is made, to or in respect of a member
of a pension scheme, by a person who is connected with the pension scheme or
10 connected with the entity in which the pension scheme has invested. Thus, in the
present case, the payment of the loan by G Loans should be regarded as a payment
made in connection with the investment made by HD SIPP in KJK only if KJK and G
Loans are connected persons within the meaning of s 161(8).

15 69. Section 161(8) cross refers to the definition of connected persons in s 993(5)
Income Tax Act 2007 which provides, broadly, that a company is connected to
another company if the same person has control of both companies or connected
persons have control of the companies. Ms Ratcliffe submits that in Mr Danvers’s
case there was no such connection between G Loans and KJK; G Loans and KJK
were independent of each other and each of them was independent of HD SIPP. The
20 FTT she submitted therefore erred in law in finding that the Loan was made in
connection with the investment in KJK.

25 70. As regards the factual position, the FTT did not explore the extent of any links
between the ownership or management of the various companies. At the hearing,
HMRC agreed that the Tribunal could consider the case on the assumption that G
Loans and KJK are not connected within the meaning of section 993 though they
made no concessions as to the position on the facts. Be that as it may, in our view this
argument is without merit. As Miss Poots submitted, s 161(8) is not relevant to the
interpretation of s 161(3). Sub-section (8) is not attempting to provide a definition for
the phrase “in connection with”, it is providing a definition for the phrase “a person
30 connected with” another person, which is needed because subsections (6) and (7) both
employ this concept. Section 161(3) is concerned with whether a payment is made in
connection with an investment and says nothing about connections between a member
of a pension scheme and any other person.

Ground 2: application to the facts of this case

35 71. Turning now to apply the proper construction of the legislation to the facts in
this case, Ms Ratcliffe submits that the FTT’s finding that the investment by the HD
SIPP in KJK was inextricably linked to the Loan and hence that the Loan was made in
connection with the investment was, in all the circumstances, a perverse and irrational
finding which no reasonable tribunal could have come to.

40 72. Ms Ratcliffe submits that the Loan and the investment in KJK were separate,
commercial transactions, the Loan was provided to Mr Danvers pursuant to terms
which reflected the commerciality of the lending, the investment in KJK was made

pursuant to the HD SIPP's powers of investment and the appropriate investment strategy for the HD SIPP, and the Loan and investment in KJK were not simultaneous with each other.

5 73. Finally, Ms Ratcliffe criticised the observations of the FTT at [2] of the Decision that the arrangements which are the subject of this appeal "constituted a version of what is commonly known as "pension liberation", i.e a structure designed to afford a pension scheme member effective access (in this case, by way of loan) to some part of his/her pension fund before the normal qualification age of 50 without incurring the income tax charges designed to deter such access."

10 74. In our view there was ample evidence from which the FTT could properly find that the investment by the HD SIPP in the KJK preference shares was inextricably linked to the Loan. It is another way of saying that Mr Danvers would not have received the Loan if he had not promised that the HD SIPP would make the investment in the KJK preference shares and it was never going to be the case that
15 having received the Loan he did not ensure that the investment was made. We have not found it necessary to make any comment as to whether these arrangements can be characterised as "pension liberation". That term has no legal significance and it may be used by different people to describe different types of arrangement. The question that we have to decide is whether these particular types of arrangement have resulted
20 in an unauthorised member payment being made within the scope of s 160(2) FA 2004 following an analysis of the arrangements in the light of the proper construction of the relevant statutory provisions.

25 75. As is apparent from the terms of the Loan summarised at [16] above, the loan agreement stated that as a condition of the loan granted Mr Danvers must transfer his existing pension funds to a SIPP with HD SIPP and after the payment of fees the remaining monies must be used to buy shares in KJK. Mr Danvers also agreed in the loan agreement not to disinvest monies from KJK or transfer monies away from the HD SIPP without the written permission of G Loans Ltd, or unless the loan is repaid in full. Breach of these conditions would lead to the loan becoming due to be repaid
30 immediately and interest to accrue at a penal rate.

35 76. On the basis of these provisions, FTT found at [59] of the Decision that the "entire arrangement was orchestrated from beginning to end to ensure that the appellant received his expected loan as a result of transferring his pension funds to the HD SIPP and instructing it to invest in the KJK preference shares." The FTT also found in the same paragraph that there was never any realistic likelihood that the transfer of Mr Danvers's pension fund to the HD SIPP would not result in the funds being invested in the KJK preference shares and Mr Danvers receiving the Loan. It also found that that was Mr Danvers's expectation. It was clear from the FTT's findings that the whole purpose of Mr Danvers transferring his pension funds to the
40 HD SIPP and directing it to invest in the KJK preference shares was so that he could obtain the Loan.

77. On the basis of those findings of fact, in our view, bearing in mind our analysis as to the meaning of "in connection with" as used in s 161(3) FA 2004, the FTT was

fully entitled to conclude as it did at [64] of the Decision that the Loan was made “in connection with” the KJK preference shares, an investment acquired using sums held for the purposes of a registered pension scheme, namely the HD SIPP.

5 78. During her submissions Ms Ratcliffe stressed the “commerciality” of the transactions described, in particular that the terms of the Loan reflected the “commerciality of the lending” and that the Loan was a commercial loan between a commercial lender and an unconnected borrower. We recognise that the Loan was ‘commercial’ in the sense that G Loans clearly intended, through the interest rate charged, to make money from the transaction. We note that some of the terms we
10 have described such as those in sub-paragraphs (9), (10) and (11) of [16] above are clearly bespoke and reflect the links between the Loan, the taking out of the pension with the HD SIPP and the investment in KJK shares. However, we do not regard the question whether the terms of the Loan were ‘commercial’ as assisting in resolving the issues before us.

15 79. The fact that Mr Danvers received the Loan on 16 December 2009 whereas the investment in the KJK preference shares was made on 17 December 2009 makes no difference to this analysis. As the FTT found, there was never any realistic possibility that Mr Danvers would not ensure that the investment in KJK preference shares was made and the terms of the loan agreement regarding early repayment were such that it
20 would clearly not have been in his interests not to follow the investment through.

80. Finally, we deal with Ms Ratcliffe’s submission that giving the provisions a broad interpretation so as to cover indirect as opposed to direct connections will result in far-reaching and unintended consequences for the lending industry. In particular, she gives the example of a loan, from a lender unconnected to a registered pension
25 scheme, advanced to a borrower on the basis that the loan might be discharged from the borrower’s pension on retirement. She submits that on a broad interpretation of the provisions, the loan would be treated as an unauthorised member payment by the registered pension scheme.

81. Ms Ratcliffe is in this example referring to a pensions mortgage, a standard
30 financial product. As we understand it, under such arrangements typically a person wishing to buy a property will finance it with a repayment mortgage in the usual way secured on the property, and it will be agreed between the borrower and the lender that the repayment date will be the borrower’s expected retirement date. This is on the basis that the borrower will expect that he will be able to draw down on his pension at
35 that point and, in particular, repay the mortgage from his tax-free lump sum. The contractual terms for such arrangements can of course take a variety of forms. The borrower may be content to rely on an expectation that the borrower will discharge the mortgage loan out of the lump sum payment or other sums available from his pension without there being any contractual obligation to do so. He may make no
40 stipulations as to who the provider of the registered pension scheme is to be or what investments may make.

82. In those circumstances, we cannot see how it could be said that the loan would be connected to any particular investment of the scheme. There is no stipulation that it

is a condition of the loan that the pension scheme invest in any particular investment so there is no causal link between the loan and the investments of the registered pension scheme.

5 83. Likewise, no causal link would in our view arise simply because the lender stipulated that the pension fund be held with a particular pension provider, or that the borrower undertake to draw down his pension on his specified retirement date and use the proceeds to repay the loan. Again, there is no causal link between the loan and any particular investment made by the registered pension scheme.

10 84. Therefore, whilst obviously each case will have to be dealt with in the light of its own particular facts, we do not believe that our findings as to the proper construction of s 161(3) and (4) FA 2004 are likely to cause difficulty with normal financial planning arrangements.

Disposition

15 85. The appeal is dismissed.

MRS JUSTICE ROSE DBE

JUDGE TIMOTHY HERRINGTON

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**UPPER TRIBUNAL JUDGES
RELEASE DATE: 10 January 2017**