UT Neutral citation number: **[2025] UKUT 59 (TCC)**

UT (Tax & Chancery) Case Number: UT/2023/000079
UT/2023/000109

**Upper Tribunal**
**(Tax and Chancery Chamber)**

*INHERITANCE TAX – sale of home by deceased to trustees of a trust in which she held an interest in possession, consideration for which was a promissory note – trustees resolved to allow deceased to continue to reside in home – gift of note by deceased to a second trust under which she was precluded from benefitting – deceased died more than seven years after this gift – FTT dismissed appeal holding that in valuing the estate the liability under the note should be abated to nil under s103 FA 1986 – Appellants appealed against that conclusion and HMRC cross-appealed on five issues – held – Note issued by the trustees was not a debt incurred by the deceased – appeal allowed, cross-appeal dismissed – decision of the FTT set aside – decision re-made – appeal allowed*

Hearing venue: The Rolls Building
London
EC4A 1NL

**Heard on:** 19 and 20 November 2024
**Written submissions:** 22 November 2024
**Judgment date:** 17 February 2025

**Before**

**JUDGE JEANETTE ZAMAN**
**JUDGE VIMAL TILAKAPALA**

**Between**

**(1) THE EXECUTORS OF MRS LESLIE VIVIENNE ELBORNE DECEASED**
**(2) THE TRUSTEE OF THE ELBORNE LIFE SETTLEMENT**
**(3) THE TRUSTEES OF THE ELBORNE FAMILY SETTLEMENT**

Appellants/Cross-Respondents

**and**

**THE COMMISSIONERS FOR HIS MAJESTY'S REVENUE AND CUSTOMS**

Respondents/Cross-Appellants

**Representation:**

For the Appellants: Charles Bradley, counsel, instructed by Buckles Solicitors LLP

For the Respondents: Jonathan Davey KC and Barbara Belgrano, counsel, instructed by the General Counsel and Solicitor for His Majesty's Revenue and Customs

## DECISION

### INTRODUCTION

1. The Appellants appeal against the decision of the First-Tier Tribunal (Tax Chamber) (the "FTT") in *The Executors of Mrs Leslie Vivienne Elborne and others v HMRC* [2023] UKFTT 626 (TC) (the "Decision") dated 14 June 2023 and oppose HMRC's cross-appeals. The Decision dismissed the appeals against notices of determination which had been issued by HMRC to the Appellants on 2 February 2017 under s221 Inheritance Tax Act 1984 ("IHTA 1984").

2. Mrs Elborne and the trustees of two trusts had, as set out further below in our summary of the Decision, entered into various transactions as part of an arrangement which was known as a "home loan scheme". Those transactions involved, in outline:

(1) the disposal by Mrs Elborne of the property in which she lived, the Old Rectory (the "Property"), to the trustees of a settlement in which Mrs Elborne had an interest in possession (the "Life Trustees" and the "Life Settlement" respectively) in exchange for a promissory note (the "Note") issued by the Life Trustees; and

(2) the assignment of the Note by Mrs Elborne by way of gift to the trustees of a settlement under which she was excluded from benefitting (the "Family Trustees" and the "Family Settlement" respectively).

3. Mrs Elborne continued to live in the Property, and died more than seven years after the gift of the Note. The Appellants' submission, before the FTT and ourselves, is that the inheritance tax consequences are:

(1) the assignment of the Note to the Family Trustees was a potentially exempt transfer, which was not chargeable as Mrs Elborne survived more than seven years after the assignment; and

(2) on Mrs Elborne's death the Property was deemed to form part of her estate (by virtue of her interest in possession in the Life Settlement) but in determining the value of her estate a deduction should be allowed for the value of the liability under the Note.

4. HMRC pursued a number of challenges before the FTT. The FTT held that a deduction for the liability under the Note was prohibited by s103 Finance Act 1986 ("FA 1986") ("s103" and the "Section 103 Debt Incurred Issue"), but found in the Appellants' favour on every other issue. The Appellants appealed on the Section 103 Debt Incurred Issue and HMRC cross-appealed on five of the issues which were decided against them by the FTT. For the reasons set out below, we have allowed the Appellants' appeal on the Section 103 Debt Incurred Issue and dismissed HMRC's cross-appeal.

5. References in this decision in the form FTT[x] are to paragraphs of the Decision.

### FTT DECISION

6. The FTT's findings of fact are detailed and address the significance (or otherwise) of various deficiencies in implementation of the transactions and the subsequent actions of some of the parties thereto, and included the following findings (at FTT[15]):

(1) Prior to 27 November 2003, Mrs Elborne lived at, and was the freehold owner of, the Property.

(2) On 27 November 2003:

(a) Mrs Elborne created the Life Settlement, the provisions of which included that Mrs Elborne was the life tenant, and "Beneficiaries" included the life tenant and the children and descendants of the life tenant;

(b) Mrs Elborne entered into a contract to sell the Property to the Life Trustees for a purchase price of £1.8m, to be satisfied by the issue of the Note (the agreed form of which was attached to the contract); and

(c) The Life Trustees resolved to purchase the Property for £1.8m, to be satisfied by the issue of the Note, and to allow Mrs Elborne to occupy the Property rent-free during her lifetime for as long as she desired.

(3) The Note issued by the Life Trustees to Mrs Elborne was dated 27 November 2003. The Note was unsecured, did not carry any interest and was freely transferable by the holder. Subject to any event of default, the Note was repayable on demand 30 days after Mrs Elborne's death or (if later) 30 days after six months had elapsed since the date of the Note. The amount to be repaid was, at the noteholder's option, (i) the nominal amount of the Note (£1.8m) index-linked by reference to changes in the retail prices index, (ii) the nominal amount of the Note, or (iii) the market value of the Note at the date of issue.

(4) There were various documents dated 8 December 2003 pursuant to which:

(a) Mrs Elborne created the Family Settlement, under which the principal beneficiaries were her three children and the provisions of which excluded Mrs Elborne from the class of beneficiaries; and

(b) Mrs Elborne assigned the Note to the Family Trustees for no consideration.

(5) On or around 15 November 2006, Mrs Elborne executed and sent to HMRC an election under paragraph 21(2) of Schedule 15 to the Finance Act 2004 ("FA 2004"). In the election, Mrs Elborne stated that the legal owners of the Property were Mr Woolfe and herself (ie the Life Trustees) and that the nature and extent of her interest in the Property was as life tenant under the Life Settlement. The covering letter included that Mrs Elborne wanted to make it clear that the Property was to be treated for the purposes of Part 5 FA 1986 as property subject to a reservation, and s102(3) and (4) FA 1986 would apply, but only insofar as she was not beneficially entitled to an interest in possession in the Property.

(6) On or around 27 January 2007, Mrs Elborne sent a revised election to HMRC. The covering letter to that revised election stated that the original covering letter still stood. In the revised election, the legal owner was stated to be Mrs Elborne. The revised election, and the terms of the original covering letter, were referred to as the "Election".

(7) Mrs Elborne continued to reside at the Property until her death on 6 January 2011.

(8) Following Mrs Elborne's death, legal title to the Property was registered at HM Land Registry in the name of Mrs Elborne's executors, and they sold the Property to unrelated third parties.

7. HMRC had instructed an expert to calculate a value for the Note on the date of its issue, and the expert's report concluded the Note would have had a value of no more than £583,500. The FTT was content to accept that valuation (FTT[16]).

8. The FTT described it as being implicit in the scheme how the sale of the Property and the receipt of the purchase price would be dealt with following Mrs Elborne's death (FTT[20]). However, the FTT found that there were "many departures" from that simple path (FTT[21]), including:

(1) various documents which bore the date 8 December 2003 were not in fact executed on that date;

(2) the Family Trustees had resolved to register a restriction over the Property, but that was never effected and could never be effected because the Property was unregistered land;

(3) Mrs Elborne's will contained a clause setting out the manner in which she wished the Property to be dealt with following her death; and

(4) Mrs Elborne's executors, rather than the Life Trustees, became the registered owners of the Property and purported to sell the Property to third parties and retain the proceeds of sale.

9. The various differences were said to have "done nothing to assist the Appellants' case", nor did the fact that the Note remained unpaid more than ten years after Mrs Elborne's death (FTT[22]). The FTT concluded that the anomalies were attributable to a combination of errors which were made in the implementation of the scheme, forgetfulness on the part of the protagonists and the advice of Mr Dumont to the effect that the Note should be left outstanding pending the outcome of the appeal (FTT[24]). The FTT found that the trust deed creating the Family Settlement, the deed of assignment of the Note and the resolution of the Family Trustees did not become effective until all of the signatories to the relevant document executed the relevant document and that this was in late January or early February 2004, ie some time after 8 December 2003 when the relevant document was dated (FTT[27]).

10. HMRC had put forward 11 arguments in support of its position that the scheme did not have the inheritance tax consequences asserted by the Appellants. The FTT decided that the Appellants' appeal should be dismissed, finding that HMRC's submissions in relation to the Section 103 Debt Incurred Issue were correct. The FTT held that a deduction for the liability under the Note was precluded by s103:

(1) the liabilities of the settlement were to be treated as having been incurred by the holder of the interest in possession, with the result that the Note was a "debt incurred by" Mrs Elborne within s103(1); and

(2) the consideration for the debt comprised "property derived from the deceased" within s103(1)(a), there being no requirement for two dispositions of property for this purpose.

**GROUNDS OF APPEAL AND CROSS-APPEAL**

11. The Appellants submit that the FTT erred in law in its conclusions on the Section 103 Debt Incurred Issue.

12. The FTT decided the remaining (ten) issues in the Appellants' favour, and HMRC cross-appealed on five of those issues:

(1) the "Section 102 Property Issue" – HMRC submit that s102 FA 1986 ("s102") applies in respect of the transfer by Mrs Elborne of her interest in the Property with the effect that such interest falls to be treated as property to which Mrs Elborne was beneficially entitled immediately before her death and forms part of the value transferred by way of the deemed transfer of value immediately before her death;

(2) the "Section 102A Issue" – HMRC submit that section 102A FA 1986 ("s102A") applies in respect of the transfer by Mrs Elborne of her interest in the Property with the effect that such interest falls to be treated as property to which Mrs Elborne was beneficially entitled immediately before her death and forms part of the value transferred by way of the deemed transfer of value immediately before her death;

(3) the "Election Issue" – HMRC submit that by virtue of making the Election Mrs Elborne brought herself within the ambit of s102 such that her interest in the Property falls to be treated as property to which Mrs Elborne was beneficially entitled immediately before her death and forms part of the value transferred by way of the deemed transfer of value immediately before her death;

(4) the "Section 49/Rossendale Issue" – HMRC submit, in part based on *Rossendale Borough Council v Hurstwood Properties (A) Ltd* [2021] UKSC 16 ("*Rossendale*"), that the liability to which the Note gave rise is not one which falls to be taken into account by way of a deduction for the purposes of s49 IHTA 1984 ("s49") having been manufactured solely for the purpose of diminishing the value of the property in which Mrs Elborne's interest in possession subsisted; and

(5) the "Section 102 Note Issue" – HMRC submit that s102 applies in respect of the transfer by Mrs Elborne of her interest in the Note with the effect that such interest falls to be treated as property to which Mrs Elborne was beneficially entitled immediately before her death and forms part of the value transferred by way of the deemed transfer of value immediately before her death.

**APPELLANTS' APPEAL ON SECTION 103 DEBT INCURRED ISSUE**

13. The Appellants submit that the FTT erred in law in its conclusions on the Section 103 Debt Incurred Issue, in particular in holding that:

(1) it is a necessary consequence of the deeming in s49(1) that the interest in possession beneficiary is deemed to have incurred debts actually incurred by the trustees;

(2) the liability under the Note was a "debt incurred by" Mrs Elborne within the meaning of s103(1); and

(3) the consideration for the debt was "property derived from" Mrs Elborne within the meaning of s103(3).

14. Whilst these grounds of appeal identified three alleged errors of law, by the time of the hearing the parties addressed (1) and (2) together and we have adopted that approach.

15. In summary, s103 involves four components:

(1) the premise of s103 is that it applies where you are determining the value of a person's estate immediately before his death;

(2) it applies where account would otherwise be taken of "a liability consisting of a debt incurred by him or an incumbrance created by a disposition made by him", with HMRC relying on the Note being "a liability consisting of a debt incurred by him";

(3) the consideration for the debt (or incumbrance) is either within s103(1)(a) or s103(1)(b), with HMRC relying on the consideration being "property derived from the deceased" within s103(1)(a), which is then defined in s103(3); and

(4) the consequence is that the liability is abated to an extent proportionate to the value of such consideration.

16. There was no dispute in relation to the application of (1) and (4) above, as it was agreed that the consequence of s103 applying would be to reduce the value of the liability, the Note, to nil as the totality of the consideration was the Property. The issues between the parties related only to (2) and (3).

17. We set out the relevant legislation, including the charging provisions within IHTA 1984, s49 and s103, summarise the parties' submissions and then set out our discussion and conclusions on the issues.

**Relevant Legislation**

18. Part 1 of the IHTA 1984 includes the main charges and definitions. Section 1 charges inheritance tax on the value transferred by a chargeable transfer. Section 3 provides that a transfer of value is a disposition made by a person as a result of which the value of his or her estate immediately after the disposition is less than it would be but for the disposition. Section 3(1) provides that, "[subject] to the following provisions of this Part of this Act, a transfer of value is a disposition made by a person (the transferor) as a result of which the value of his estate immediately after the disposition is less than it would be but for the disposition; and the amount by which it is less is the value transferred by the transfer."

19. Section 4(1) provides that, "[on] the death of any person tax shall be charged as if, immediately before his death, he had made a transfer of value and the value transferred by it had been equal to the value of his estate immediately before his death."

20. Section 5 sets out the meaning of the word "estate" and provides, so far as relevant, as follows:

> "5(1) For the purposes of this Act a person's estate is the aggregate of all the property to which he is beneficially entitled…
>
> (3) In determining the value of a person's estate at any time his liabilities at that time shall be taken into account, except as otherwise provided by this Act…
>
> (5) Except in the case of a liability imposed by law, a liability incurred by a transferor shall be taken into account only to the extent that it was incurred for a consideration in money or money's worth."

21. Part 3 contains provisions dealing with settled property, Chapter 2 of which relates to interests in possession, reversionary interests and settlement powers. Within that Chapter, s49(1) provides as follows:

> "49(1) A person beneficially entitled to an interest in possession in settled property shall be treated for the purposes of this Act as beneficially entitled to the property in which the interest subsists."

22. Part 6 contains provisions dealing with valuation. Section 160 provides:

> "160 Except as otherwise provided by this Act, the value at any time of any property shall for the purposes of this Act be the price which the property might reasonably be expected to fetch if sold in the open market at that time; but that price shall not be assumed to be reduced on the ground that the whole property is to be placed on the market at one and the same time."

23. Section 162 provides, so far as relevant:

> "162(1) A liability in respect of which there is a right to reimbursement shall be taken into account only to the extent (if any) that reimbursement cannot reasonably be expected to be obtained…
>
> (4) A liability which is an incumbrance on any property shall, so far as possible…, be taken to reduce the value of that property."

24. Section 103 FA 1986 is headed "Treatment of certain debts and incumbrances" and provides, so far as relevant, as follows:

> "103(1) Subject to subsection (2) below, if, in determining the value of a person's estate immediately before his death, account would be taken, apart from this subsection, of a liability consisting of a debt incurred by him or an incumbrance created by a disposition made by him, that liability shall be subject to abatement to an extent proportionate to the value of any of the consideration given for the debt or incumbrance which consisted of -
>
> (a) property derived from the deceased; or
>
> (b) consideration (not being property derived from the deceased) given by any person who was at any time entitled to, or amongst whose resources there was at any time included, any property derived from the deceased….
>
> (3) In subsections (1) and (2) above "property derived from the deceased" means, subject to subsection (4) below, any property which was the subject matter of a disposition made by the deceased, either by himself alone or in concert or by arrangement with any other person or which represented any of the subject matter of such a disposition, whether directly or indirectly, and whether by virtue of one or more intermediate dispositions…
>
> (6) Any reference in this section to a debt incurred is a reference to a debt incurred on or after 18th March 1986 and any reference to an incumbrance created by a disposition is a reference to an incumbrance created by a disposition made on or after that date;....."

**Decision of the FTT**

25. Before addressing the Section 103 Debt Incurred Issue in its Decision, the FTT had first made what it described as observations about the decision of Mann J in *St Barbe Green v HMRC* [2005] EWHC 14 (Ch) ("*St Barbe Green*") "given the significance of that decision" to this issue and to the Section 102 Property Issue (which is one of the issues in HMRC's cross-appeal). The facts of that case were summarised by the FTT:

> "121. In *St Barbe Green*, the deceased's free estate (as opposed to his interests as life tenant in certain settlements) had more liabilities than assets. The issue in the case was whether the excess of the liabilities over the assets in his free estate could be used to reduce the value of the assets in the settlements (that fell to be treated as part of his estate pursuant to Section 49). The trustees argued that the effect of Section 5(3), which provided that, in determining the value of a person's estate, the person's liabilities were to be taken into account, except as otherwise provided by the IHTA, meant that the trustees were entitled to set off the value of the excess liabilities in the deceased's free estate against the value of the assets in the settlements. Mann J held that they could not."

26. The FTT summarised the reasoning of Mann J:

> "122. His main reason for reaching this conclusion turned on the use of the word "property" in Sections 5(1) and 49. He held that the reference in Section 49 to "property" must necessarily mean "net property", which is to say the value of the settlement assets minus the value of the settlement liabilities. It followed that the same interpretation of the word "property" must be applied in Section 5(1), with the result that the property of the free estate which was brought into account under that section must also be the net property – the value of the assets in the free estate minus the value of the liabilities in the free estate. It followed that Section 5(3) played no positive role in the process of deducting liabilities in calculating the value of a person's estate. Its role was in part merely confirmatory of the principle that the property to be brought into account under the sections was the net property but its main purpose was to make it clear that, in calculating the value of the net property for the

purposes of each of Sections 5(1) and 49, there were certain liabilities which might be precluded from being deducted."

27. The FTT then addressed Mr Bradley's submissions:

> "125. At the hearing, Mr Bradley submitted that there were three points of principle in relation to the application of Section 49 which could be derived from the decision in *St Barbe Green*, as follows:
>
> (1) first, the reason why settlement liabilities are deductible in determining the value of the settled property to which the deceased was entitled under Section 49 is not Section 5(3) but simply the meaning of the word "property" in Section 49 itself;
>
> (2) secondly, it follows from this that, where the deceased had an interest in possession in settled property so that the settled property is to be brought into his estate by Section 49, that section does not deem the deceased to have incurred the liabilities to which the settlement was subject. Instead, it is simply the case that the value of the property to which the deceased is to be treated as being entitled under that section is to be calculated after taking into account the value of the settlement liabilities; and
>
> (3) thirdly, that process is simply a means of calculating the value of the property which should be taken into account pursuant to Section 49. It does not mean that the deceased is to be treated as having no beneficial entitlement to the portion of the assets in the settlement that does not exceed the settlement liabilities.
>
> 126. We agree with Mr Bradley's first point but we think that there is quite an uneasy relationship between the other two. That is because, if the effect of the section is to bring into the deceased's estate only the net value of the property in the settlement, then that must either mean that the deceased is to be treated as having had no beneficial entitlement to the portion of the gross settled property which did not exceed the settlement liabilities (so that the third proposition is wrong) or that the deceased is to be treated as having had a beneficial entitlement to the gross settled property but as being entitled to deduct the settlement liabilities in calculating the value of that beneficial entitlement (so that some strain is being placed on the second proposition).
>
> 127. We agree with Mr Bradley's third proposition. That is because, in the passage from the case set out above, Mann J refers to the settled property as being "property from which liabilities have been notionally deducted". It therefore seems to us to be clear that the deduction of settlement liabilities is a matter which goes to calculating the value of the property to which the deceased is to be treated as being beneficially entitled as opposed to the identification of the property to which the deceased is to be treated as being beneficially entitled. We would add that further support for that proposition is to be derived from the terms of paragraph 11 of Schedule 15 to the FA 2004 because it is clear from the language in paragraph 11(6) of that schedule that a liability which affects the value at which property is to be brought into account in calculating the value of a person's estate does not prevent the part of the property which does not exceed that liability from being part of the estate. Otherwise, paragraph 11(6) would not have been needed.
>
> 128. We can also see how Mr Bradley's second proposition might be correct but that turns on the extent of the implications to be drawn from the process of deduction which is a necessary part of the valuation process. We can see how, in theory, it might be possible to take settlement liabilities into account in valuing the property to which the deceased is to be treated as being

> beneficially entitled without specifically treating those liabilities as having been incurred by the deceased. But, in light of the third proposition, pursuant to which it is accepted that the deceased is to be treated pursuant to Section 49 as having a beneficial entitlement to the gross settled property (and not merely the portion of the gross settled property which exceeds the settlement liabilities), it is tempting, to say the least, to conclude that the liabilities should be deemed to have been incurred by the deceased.
>
> 129. We will return to this dichotomy when we address the relevant issues below."

28. The FTT's reasoning on the Section 103 Debt Incurred Issue was then as follows:

(1) Section 49 does not say expressly that the liabilities incurred by the trustees of a settlement should be treated as having been incurred by the holder of the interest in possession in the settlement (FTT[226]).

(2) There is "a necessary implication in the language of [s49] that the debts of the settlement should be treated as having been incurred by the person owning the interest in possession" (FTT[228]). The FTT's reasoning was:

> (a) Mann J saw s49 as bringing within the estate the whole of the settled property in which the deceased had an interest in possession but as requiring the settlement liabilities to be deducted. The effect of s49 is to confer deemed beneficial ownership of the gross settlement assets but to take into account in valuing those assets the liabilities of the settlement. Mann J was not saying that the effect of s49 was that the deceased did not have an interest in possession in the portion of the gross settlement assets which did not exceed the liabilities of the settlement. Mann J was saying that the effect of the section was to confer on the holder of an interest in possession deemed beneficial ownership of the gross settlement assets but to take into account in valuing those assets the liabilities of the settlement.
>
> (b) Since that is the effect of s49, who else apart from the holder of the interest in possession should be treated as having incurred those liabilities which are to be taken into account in reducing the value of gross settled assets? Those assets are deemed to be beneficially owned by the holder of the interest in possession but to have a reduced value to that holder by reference to the liabilities in question. A necessary implication arising from that process is that the liabilities have been incurred by the holder of the interest in possession (FTT[228]).
>
> (c) Since there is this necessary implication in the language of s49, it is then necessary to apply the principles set out by Lord Briggs in *Fowler v HMRC* [2020] UKSC 22 ("*Fowler*") again, in determining whether that deeming should be carried across when construing s103. That is the case; it is a consequence which flows inevitably from assuming the fiction implicit in s49 to be real, and extending that consequence does not produce an unjust, absurd or anomalous result. Extending the fiction means that s103 is fulfilling its manifest purpose (FTT[230]).

(3) Given that the amount by which the value of the liability under the Note is to be abated is the amount of the consideration which was provided by Mrs Elborne for the issue of the Note – which is to say the value of the Property at the time when the Sale Agreement was executed and the Note was issued – the amount of the liability under the Note should be abated to nil (FTT[234]).

(4) There is no need for there to be two dispositions of property in a case where Section 103 is being invoked by reference to the existence of a debt incurred (as opposed to being invoked by reference to the creation of an incumbrance) (FTT[235]). (The FTT had

concluded in the context of the Section 103 Incumbrance Issue at FTT[214] that the language of the section was such that there is a clear and obvious separation between the disposition which created the incumbrance and the disposition of the property which was, or was represented by the property which was, the consideration for the creation of the incumbrance.)

**Summary of parties' submissions**

29. Mr Bradley submitted that:

(1) s103(1) requires that the deceased must himself have incurred a debt – here, the liability under the Note was not a "liability consisting of a debt incurred by [Mrs Elborne]"; the liability had been incurred by the Life Trustees. Section 49(1) merely said that a person holding an interest in possession should be deemed to be beneficially entitled to the property in which that interest subsisted, and the decision in *St Barbe Green* had made it clear that that property was to be valued net of the settlement liabilities. Section 49(1) did not deem the person with the interest in possession to have incurred the debts of the settlement, and no such deeming should be treated as applying for the purposes of s103. Section 60 Taxation of Chargeable Gains Act 1992 ("TCGA 1992") illustrates that it is not be difficult for Parliament to say expressly what the FTT thought it had said by implication. The approach of the FTT and the dichotomy (which he described as a false dichotomy) which it had identified at FTT[125] to FTT[129] raised difficult and fundamental questions as to how trust liabilities are taken into account for inheritance tax purposes, given that s49 only applies where there is "an interest in possession in settled property" and cannot therefore apply to bare trusts or discretionary trusts; and

(2) s103 requires that the deceased must, by some prior disposition(s) have furnished someone else with the property used as consideration for that debt (or incumbrance) - Mr Bradley submitted that this meant that the Property itself could not fulfil this requirement. There needed first to have been a disposition of property by the deceased and then that property (or property representing that property) needed to be used as consideration for the debt. Mr Bradley drew attention to the different conclusion which the FTT had reached on this submission in the context of the Section 103 Incumbrance Issue.

30. At the beginning of his oral submissions at the hearing, Mr Davey drew our attention to the context in which this appeal arose, emphasising:

(1) Mrs Elborne had entered into a scheme to reduce the liability of her estate to inheritance tax, the "home loan scheme";

(2) the witness evidence of Mr Mark Elborne (one of Mrs Elborne's children, who was a beneficiary of both settlements, a Family Trustee and an executor under Mrs Elborne's will) was that the sole purpose of entering into the scheme had been to remove the value of the Property from his mother's estate (assuming she was able to survive for more than seven years);

(3) that scheme involved multiple documents being executed (including the creation of the two trusts, an agreement for sale, the Note, letters of wishes and trustee resolutions); and

(4) there had been no transfer of funds (either physical cash or electronic transfer), the agreement for sale of the Property was not completed, the scheme documentation was essentially ignored, following Mrs Elborne's death the executors simply sold the Property to a third party directly, and the Note has not been repaid. In the real world, nothing actually changed – Mrs Elborne continued to live at the Property, there were no

proceeds of sale in a bank account, and no changes recorded at the Land Registry (although noting that the Property was unregistered property).

31. Against this background, Mr Davey submitted that the Note does not operate as a "magical device" to swerve the statutory provisions and reduce the value of the estate by £1.8m.

32. Mr Davey addressed the application of s103, submitting that this is generally regarded as an anti-avoidance provision. We should not narrow the scope of this provision by reference to an example of when the provision can apply (eg to loan-backs). The FTT had concluded that their approach fulfilled the "manifest purpose" of the provision (FTT[230]).

33. Mr Davey addressed the reasoning of the FTT from FTT[226] to FTT[233] on whether the Note was a "debt incurred by" Mrs Elborne:

(1) The FTT had recognised that s49 does not say expressly that the liabilities incurred by the trustees should be treated as having been incurred by the holder of the interest in possession in the settlement (FTT[226]).

(2) The FTT set out its analysis at FTT[228], which HMRC broke down into three parts:

(a) Mann J saw s49 as bringing within the estate the whole of the settled property but as requiring the settlement liabilities to be deducted in valuing that property. Mann J was not saying that the effect was that the deceased did not have an interest in possession in the portion of the gross settlement assets which did not exceed the liabilities of the settlement.

(b) Since that is the effect of s49, who else apart from the deemed beneficial owner of the gross settled assets should be treated as having incurred the relevant liabilities which are to be taken into account in reducing the value of the gross settled assets.

(c) Those assets are deemed to be beneficially owned by the holder of the interest in possession but to have a reduced value to that holder by reference to the liabilities. A necessary implication arising from that process is that the liabilities have been incurred by the holder of the interest in possession.

(3) The FTT saw its conclusion as in line with *St Barbe Green* (FTT[233]).

(4) In *St Barbe Green*, Mann J held that liabilities in the free estate could not be used to reduce the value of the surplus assets held in trusts. Mann J had addressed s49 at [12], stating that whilst s49(1) does not say "net property" (ie the value of the property net of trust liabilities) that is what it must mean, thus it has the "notion of property from which liabilities have been notionally deducted".

(5) Mr Davey submitted that liabilities cannot be disregarded under s49. Section 49 is a deeming provision. At [11] in *St Barbe Green*, Mann J had described the statute as creating "its own logical world" by deeming trust property to be owned by the deceased. In *Fowler*, Lord Briggs had set out the guidance as to the way in which statutory deeming provisions ought to be interpreted and applied, the fifth principle of which (at [27(5)]) is that "the court should not shrink from applying the fiction created by the deeming provision to the consequences which would inevitably flow from the fiction being real". The FTT had considered that the effect of s49 was that Mrs Elborne was to be treated as having incurred the debt owed by the Life Trustees. It is then an incident of the consequences of that deeming to interpret Mrs Elborne as having incurred that debt for the purposes of s103(1).

34. Addressing the further submissions made by the Appellants, Mr Davey submitted:

(1) We should beware of Mr Bradley's submissions as to the dichotomy apparently identified by the FTT in relation to trust liabilities and how such liabilities might be taken into account in different situations. The Appellants are wrong to say that the source of the right to deduct trust liabilities can be explained in all situations by s162(4). That provision addresses certain deductible liabilities (that they should be set "so far as possible" against the properties they incumber) and is not itself dealing with the prior question of whether the liability is deductible. There are a plurality of provisions performing different roles (including s5(3), s49(1) and s162); the inheritance tax code is not straightforward and a number of provisions might have a bearing. In any event, the FTT was very clear that it was dealing with the sections before it and the facts in these appeals.

(2) As regards the treatment of liabilities for other trusts, when establishing the value of the property to which the person is beneficially entitled (in the case of a bare trust) and property to which the person is deemed to be beneficially entitled (by s49), applying *St Barbe Green*, liabilities can be deducted and those liabilities are also subject to the other provisions, including s103. Consistently with the language and structure of s64 IHTA 1984, trustee liabilities can be deducted in calculating the "value" of the relevant property for the purposes of calculating the ten-year charge on settlements without an interest in possession. Section 60 TCGA 1992 cannot assist, as it is a differently worded section within a different tax regime. We need to focus on construing the provisions in front of us in this appeal.

(3) To the extent that the Appellants submit that the deeming in s49(1) should not be applied for the purposes of s103, that begs the question by assuming the validity of the Appellants' position on the structure and purpose of s103.

(4) There is nothing self-defeating or anomalous in applying the deeming to s103 in the manner set out by the FTT. The effect is that, had Mrs Elborne not transferred the Note to the Family Settlement, her estate would have had equal and offsetting assets and liabilities represented by the Note (subject to any provisions requiring that the liability not be taken into account).

35. Addressing the Appellants' alternative submission that the consideration for the Note was not "property derived from" Mrs Elborne for the purposes of s103, Mr Davey submitted that s103 does not require two separate transactions. The FTT had rightly rejected this argument, having stated at FTT[212] (in the context of the Section 103 Incumbrance Issue) that "the use of the past tense is adequately explained by the fact that Section 103 is necessarily looking back in time from the point immediately before the deceased's death". He submitted that the Appellants' argument seeks to cut down the meaning of "property derived from the deceased" in a manner which is inconsistent with the meaning of that phrase (including as defined in s103(3)) and with the purposive construction intended for an anti-avoidance provision.

36. Mr Davey submitted that the Appellants' approach gives rise to the peculiar consequence identified by the FTT at FTT[235], namely "it would be very peculiar if the application of the Section were to turn on the fact that the consideration given for the issue of the Note was provided simultaneously with, and not a scintilla of time before, the issue of the Note".

37. In addition, Mr Davey submitted that the Appellants' contention is inconsistent with *McDougal's Trustees v The Lord Advocate* [1952] SC 260 ("*McDougal's Trustees*"), where Lord Patrick, addressing the predecessor provision to s103 which applied to estate duty, addressed a gift and loan which were said to be "related in the closest possible way" as they

"formed part of one transaction" (at p276) and said these facts did not prevent the application of case (b) of (what was then) s31(1) Finance Act 1939 ("FA 1939") to the debt in question.

38. The Appellants had submitted that their approach was consistent with the purpose of limb (a). Mr Davey submitted that this takes the position no further where there is no universally agreed purpose.

39. Mr Bradley had contrasted the FTT's approach to debt cases with that which it had taken in respect of incumbrance cases, where the FTT had concluded at FTT[214] that the language of s103 is such that there is a "clear and obvious" separation between the disposition which created the incumbrance and the disposition of the property which was, or was represented by the property which was, the consideration for the creation of the incumbrance. Whilst HMRC are not cross-appealing the FTT's decision on the Section 103 Incumbrance Issue, Mr Davey confirmed that HMRC's position is that the FTT's analysis on the incumbrance limb was erroneous. They therefore agree with the Appellants that the language concerning the creation of an incumbrance in s103(1) does not justify the separation which was read in by the FTT in the context of the Section 103 Incumbrance Issue.

**Discussion**

40. The Appellants submit that the FTT's decision on the Section 103 Debt Incurred Issue involved two errors of law, each of which is such that, if made out, the Appellants' appeal should be allowed.

***"Debt incurred by"***

41. We address first the question whether the liability under the Note was a "debt incurred by" Mrs Elborne for the purposes of s103. The parties agreed for this purpose that the liability represented by the Note would (apart from this section) be taken into account in determining the value of Mrs Elborne's estate immediately before her death.

42. It is readily apparent from the facts that the Note was issued by the Life Trustees, not by Mrs Elborne, and this is why the focus of the parties' submissions, and the Decision, is on the deeming in s49(1) - both the meaning and extent of that section and how it applies, if at all, when interpreting s103. Both parties addressed the decision in *St Barbe Green*, the statutory provisions potentially relevant to the deduction of trust liabilities and the leading authorities relevant to the approach to be taken to deeming provisions.

43. We start with s49(1) itself. Section 49(1) provides that "A person beneficially entitled to an interest in possession in settled property shall be treated for the purposes of this Act as beneficially entitled to the property in which the interest subsists". It was common ground that Mrs Elborne, as holder of the interest in possession of the Life Settlement, was thus to be treated as beneficially entitled to the property in which her interest subsisted.

44. The meaning of this provision was considered in *St Barbe Green*, albeit that the question in that case arose out of how and in relation to what s5(3) operates.

45. In *St Barbe Green*, the argument for the trustees was summarised at [8] as being that the effect of s5(3) is simple; it contains the mandatory word "shall", operates in relation to "a person's estate" which means the aggregated estate (ie the free estate and the settled funds), so that after exhausting the limited assets in the free estate the balance of the liabilities in the free estate is available to reduce the assets in the settled funds.

46. HMRC's approach in that case was that s5(3) is concerned with determining value, and that in determining value one takes into account liabilities so far as those liabilities fell to be met out of that estate ([9]). The way one does this is to deduct them from the value of the property which is answerable to those liabilities. Only the assets in the free estate were

answerable in law for the free estate's liabilities - since the trust assets were not available to pay the deceased's personal liabilities, the personal liabilities could not be offset against the trust assets for inheritance tax purposes.

47. Mann J set out the reasons for his decision as follows:

> "11…The statute has created its own logical world by deeming trust property to be owned by the deceased…
>
> 12. Having said that I consider that the Inland Revenue's overall contention (that the net liabilities are not available to reduce the estate beyond the value of the free estate's assets that are liable to meet them) is right when the statute is looked at correctly. Inheritance tax is charged on death by virtue of the deemed transfer of value in section 4. That is a transfer of value "equal to the value of [the deceased's] estate immediately before his death". His estate is the "aggregate of all property to which he is beneficially interested". The word "property" is important here. It is not defined for these purposes (section 272 of the Act contains a partial definition in it that states what the expression includes but not what it means), but it is important to note that section 49(1) (which brings in the settled assets) does so by deeming the deceased to be beneficially entitled to "the property" in which his life interest subsists. It does not say "net property" (ie the value of the property net of trust liabilities) but that is what it must mean, and the parties to this appeal both agree that in practice that is the effect the Revenue gives to the section. Thus in section 49(1) we have the notion of property from which liabilities have been notionally deducted. That notion can be applied in section 5(1), so that the property of the deceased which is brought into the aggregation is his personal estate net of his liabilities. In other words, it is at that stage that the liabilities are dealt with. It is not necessary for section 5(3) to provide for a second time that the debts are to be deducted in arriving at the value of the deceased's property (or estate) and in my view it is not really doing that. It is in part confirmatory, but in the main it is intended to provide a qualification or qualifications to the principle that debts are deductible – the meat of the subsection is in the closing words "except as otherwise provided by this Act". One finds provisions in the Act which qualify that right in sections 5(4), 5(5) and 162. Its confirmatory nature is supported by the use of the phrase "taken into account", which is more general than "shall be deducted". I accept that the nature of section 5(3) would be clearer without the comma, but nevertheless it seems to me to be clear enough. This way of reading the Act enables consistency to be achieved in relation to the use of the word "property" in section 49 and section 5(1). It means that section 5(3) does not have the effect contended for by the trustees, and the Revenue is right in its conclusion. The personal estate comprises the property in it net of liabilities; once it is reduced to zero by those liabilities its value cannot decline further, and any additional liabilities have nothing against which they can be offset. The zero sum is aggregated with the settled property (net of trust liabilities) which is brought in by section 49(1).
>
> 13. This is not the line of the reasoning of the Inland Revenue, though it arrives at the result that it contends for. However, if my reasoning is wrong, then I nevertheless consider that the approach of the Revenue, which is to consider the words "taken into account" is correct in the alternative, and this leads to the same conclusion. The argument of the Revenue, it will be remembered, is that one takes liabilities into account

> by off-setting them against assets out of which they can properly be met, but no further because that is what section 5(3) provides... "

48. From this (and responding to Mr Bradley's submissions at the hearing), the FTT's reasoning was:

> (1) This must either mean that the deceased is to be treated as having had no beneficial entitlement to the portion of the gross settled property which did not exceed the settlement liabilities or that the deceased is to be treated as having had a beneficial entitlement to the gross settled property but as being entitled to deduct the settlement liabilities in calculating the value of that beneficial entitlement (FTT[126]).
>
> (2) It is clear from Mann J's reference to the settled property as being "property from which liabilities have been notionally deducted" that the deduction of settlement liabilities is a matter which goes to calculating the value of the property to which the deceased is to be treated as being beneficially entitled as opposed to the identification of the property (FTT[127]).
>
> (3) In theory, it might be possible to take settlement liabilities into account in valuing the property to which the deceased is to be treated as being beneficially entitled without specifically treating those liabilities as having been incurred by the deceased. But it is tempting, to say the least, to conclude that the liabilities should be deemed to have been incurred by the deceased (FTT[128]).
>
> (4) There is a necessary implication in the language of s49 that the debts of the settlement should be treated as having been incurred by the person owning the interest in possession - who else apart from the holder of the interest in possession should be treated as having incurred the liabilities which are to be taken into account in reducing the value of the gross settled assets (FTT[228]).
>
> (5) That deeming should then be carried across when construing s103 (FTT[230]).

49. Mr Bradley made it clear that the Appellants agreed with the FTT when it had said (based on its summary of Mann J's reasoning at FTT[127], which formed part of its own subsequent reasoning in FTT[228]) that the effect of s49(1) was to confer on the holder of an interest in possession deemed beneficial ownership of the gross settlement assets but to take into account in valuing those assets the liabilities of the settlement.

50. Mr Bradley took issue with the conclusions which the FTT had then reached from this (also in FTT[228]). Mr Bradley submitted that the approach taken by the FTT when asking and answering the question - who else (apart from the holder of the interest in possession) should be treated as having incurred the liabilities? - was based on the premise that attributing the trust liabilities to the holder of the interest in possession was the only way they could be taken into account. He submitted that this was an error of law. Mr Bradley submitted that if this was not the basis for the FTT's decision, then the "necessary implication" found by the FTT was simply an assertion that it follows from s49(1) that the holder of the interest in possession is also treated as personally liable. This does not follow and, he submitted, is inconsistent with the decision in *St Barbe Green* where, if the deceased was to be treated as personally liable for trust liabilities as well as those in the free estate, trust liabilities would also have been "his liabilities" within s5(3).

51. We start from the position that s49(1) does not make any express provision in relation to the liabilities of the settlement. Mann J had treated it as making provision for the deduction of settlement liabilities when calculating the *value* of the property to which the deceased is to be treated as being beneficially entitled. However, neither the language of s49(1) nor the decision in *St Barbe Green* makes any reference to the parties to those liabilities (including whether the

holder of the interest in possession is to be treated as owing or having incurred the trust liabilities).

52. We do not agree with Mr Bradley that the FTT was proceeding on the basis that attributing the trust liabilities to the holder of the interest in possession was the only way they could be taken into account. The FTT had, at FTT[128], acknowledged that "in theory" it might be possible to take liabilities into account without treating them as having been incurred by the deceased, and had then said that it was "tempting, to say the least" to conclude that they should be deemed to have been incurred by the deceased. The FTT thus set out its reasoning expressly and this does not support Mr Bradley's submission that the FTT had thought that this was the only way the trust liabilities could be taken into account. Whilst both parties made submissions as to how liabilities of different types of trusts are to be taken into account, we consider that it is unnecessary in the context of this appeal to set out how the provisions may operate in other contexts or in relation to different types of trusts. We agree with Mr Davey that there is a plurality of provisions which may be relevant – as can be illustrated by the alternative approaches considered by Mann J at [12] and [13] - and which perform different functions, including s5(3), s49(1) and s162 IHTA 1984 and s60 TCGA 1992.

53. Addressing whether settlement liabilities are, by necessary implication, to be treated as having been incurred by the holder of the interest in possession by s49(1), and whether this outcome should then apply for the purposes of s103, Mr Bradley referred us to *R (Morgan Grenfell & Co Ltd) v Special Commissioner of Income Tax* [2002] UKHL 21 ("*Morgan Grenfell*") and *Mark McLaren Class Representative Ltd v Nippon Yusen Kabushiki Kaisha* [2023] EWCA Civ 1471 ("*McLaren*").

54. In *Morgan Gren*fell, HMRC sought the consent of the special commissioner to issue a notice under s20(1) Taxes Management Act 1970 ("TMA 1970") requiring disclosure by the bank of its legal advice. The bank submitted that relevant consent should not be given because a s20(1) notice could not require disclosure of documents covered by legal professional privilege. HMRC submitted that other provisions expressly preserved certain categories of privileged documents from disclosure, whereas s20(1) contained no such exclusion. The House of Lords held that legal professional privilege was a fundamental human right that could be overridden only by express words or necessary implication; s20(1) did not exclude it expressly, and it was not a necessary implication from the structure of TMA 1970 as a whole that it was intended to be overridden in respect of a notice under s20(1). Lord Hobhouse's speech included the following:

> "45. It is accepted that the statute does not contain any express words that abrogate the taxpayer's common law right to rely upon legal professional privilege. The question therefore becomes whether there is a necessary implication to that effect. A necessary implication is not the same as a reasonable implication…A *necessary* implication is one which necessarily follows from the express provisions of the statute construed in their context. It distinguishes between what it would have been sensible or reasonable for Parliament to have included or what Parliament would, if it had thought about it, probably have included and what it is clear that the express language of the statute shows that the statute must have included. A necessary implication is a matter of express language and logic not interpretation."

55. More recently, in *McLaren*, Popplewell LJ explained this as follows:

> "43. Where a meaning is not set out expressly in the wording of the instrument, that meaning may nevertheless sometimes be implied. However, where the instrument is silent, the implication must be a necessary one, not merely reasonable or desirable…The test is one of necessity, and that this means is

> that the implication must be "compellingly clear": B (A Minor) v Director of Public Prosecutions…
>
> 44. One reason for such an approach is that it is a relevant factor against making the implication if it would have been easy enough for the instrument to have said it expressly but did not do so…"

56. Mr Bradley submitted that the implication drawn by the FTT was not necessary on this basis. Furthermore, he submitted that it is relevant that s60 TCGA 1992 illustrates that it would have been easy enough for Parliament to have said this expressly if this had been its intention.

57. Both parties referred us to the decision of the Supreme Court in *Fowler v HMRC* [2020] UKSC 22 ("*Fowler*") where Lord Briggs (with whom Lord Hodge, Lady Black, Lady Arden and Lord Hamblen agreed) set out the following guidance:

> "27. There are useful but not conclusive dicta in reported authorities about the way in which, in general, statutory deeming provisions ought to be interpreted and applied. They are not conclusive because they may fairly be said to point in different directions, even if not actually contradictory. The relevant dicta are mainly collected in a summary by Lord Walker in *DCC Holdings (UK) Ltd v Revenue and Customs Comrs* [2011] 1 WLR 44, paras 37-39, collected from *Inland Revenue Comrs v Metrolands (Property Finance) Ltd* [1981] 1 WLR 637, *Marshall v Kerr* [1995] 1 AC 148; 67 TC 56 and *Jenks v Dickinson* [1997] STC 853. They include the following guidance, which has remained consistent over many years:
>
> (1) The extent of the fiction created by a deeming provision is primarily a matter of construction of the statute in which it appears.
>
> (2) For that purpose the court should ascertain, if it can, the purposes for which and the persons between whom the statutory fiction is to be resorted to, and then apply the deeming provision that far, but not where it would produce effects clearly outside those purposes.
>
> (3) But those purposes may be difficult to ascertain, and Parliament may not find it easy to prescribe with precision the intended limits of the artificial assumption which the deeming provision requires to be made.
>
> (4) A deeming provision should not be applied so far as to produce unjust, absurd or anomalous results, unless the court is compelled to do so by clear language.
>
> (5) But the court should not shrink from applying the fiction created by the deeming provision to the consequences which would inevitably flow from the fiction being real. As Lord Asquith memorably put it in *East End Dwellings Co Ltd v Finsbury Borough Council* [1952] AC 109, at 133:
>
> "The statute says that you must imagine a certain state of affairs; it does not say that having done so, you must cause or permit your imagination to boggle when it comes to the inevitable corollaries of that state of affairs.""

58. Applying these principles (and noting that the numbering of the sub-paragraphs below is not intended to correlate to the numbering used by Lord Briggs):

> (1) Mann J had described IHTA 1984 as having "created its own logical world by deeming trust property to be owned by the deceased" ([11]). On its own, this is no more than a recognition that s49(1) is a deeming provision.
>
> (2) Looking at s49 in the context of IHTA 1984, the charging provision is s4, which is expressed by reference to the value of the estate immediately before death. Section 5(1) provides that a person's estate is "the aggregate of all the property to which he is

beneficially entitled", and s5(3) provides "In determining the value of a person's estate at any time his liabilities at that time shall be taken into account, except as otherwise provided by this Act". Section 49 then sits within Chapter 2 of Part 3, dealing with settled property, and uses the language of beneficial entitlement, which had also been used in s5(1), and it is this provision which, as identified by Mann J at [12], brings the settled property into the estate of the holder of the interest in possession.

(3) Having applied the deeming in s49(1) for this purpose of bringing the settled property into the estate of the holder of the interest in possession, there is no obvious need for s49(1) to be given a construction which goes beyond this. Parliament could have said expressly that liabilities incurred by the trustee were to be treated as liabilities of the holder of the interest in possession, but it did not do so. It was in any event not necessary for them to have done so to ensure that settled property was brought within that holder's estate.

(4) We have considered whether the fourth and fifth principles in *Fowler* may provide further assistance. They offer a warning and encouragement respectively to a court or tribunal when applying a statutory fiction.

(5) The fourth principle warns that a deeming provision should not be applied so as to produce unjust, absurd or anomalous results, unless the court is compelled to do so by clear language. We do not agree with Mr Bradley that it would be absurd or nonsense to treat Mrs Elborne as being liable under the Note just because it had initially been issued to her as consideration for the sale of the Property – as Mr Davey submitted, in this scenario it would simply have meant that, had Mrs Elborne not assigned the Note to the Family Settlement, her estate would have included an offsetting asset and liability.

(6) The fifth principle emphasises that a court should not shrink from applying the fiction created by the deeming provision to the consequences which would inevitably flow from the fiction being real. This principle would support the state of affairs which is deemed to exist by reason of s49(1) being applied when interpreting and applying other provisions, including s103.

(7) However, the difficulty faced by HMRC is that whilst we are satisfied that the guidance in *Fowler* would support an approach which means that the "logical world" provided for by s49(1) should be read across and applied to other statutory provisions where this reflects the inevitable consequences or corollaries of such a state of affairs, particularly where this assists with giving effect to the purpose of anti-avoidance provisions, and the result would not lead to absurdity, we do not agree with HMRC as regards the interpretation of s49(1) itself. We are not persuaded that the deeming in s49(1) requires that the holder of the interest in possession be treated as personally liable for the debts of the settlement. Viewing s49(1) in its statutory context, it is not necessary to impose such a construction on the language of the provision – the provision makes sense, and fulfils its statutory purpose, as interpreted by Mann J in *St Barbe Green*, in that it operates to bring the settled property into the estate of the holder of the interest in possession. The "notion of property from which liabilities have been notionally deducted" (at [12]) does not require that settlement liabilities are treated as being the liabilities of anyone other than, here, the Life Trustees. Section 49(1) should not be construed in a way which forces it to answer a different question, which is one which there is no evidence that Parliament had intended it should answer.

59. We therefore conclude that the FTT made an error of law when it concluded that it is a necessary implication in the language of s49(1) that debts of the settlement should be treated as having been incurred by the holder of the interest in possession. It follows from this

conclusion that the FTT's decision that such deeming should then be carried across when construing s103 involved an error of law.

***"Property derived from"***

60. The Appellants submitted that the FTT had made a further error of law in concluding that the consideration for the debt was "property derived from" Mrs Elborne within the meaning of s103(3). This submission would only be relevant if the liability under the Note is a debt incurred by Mrs Elborne for the purpose of s103(1).

61. Mr Bradley submitted that s103(1)(a) (the only limb relied upon by HMRC) looks at the property given as consideration by the counterparty for the transaction and asks whether that property was the subject-matter of a disposition made by the deceased. He submitted that as a matter of structure and logic, the disposition in s103(3) must be a different transaction from that in s103(1), otherwise, if the disposition hasn't already happened, the property is not available to be given as consideration. The use of the past tense in s103(3) is a function of this structure.

62. Mr Bradley submitted that an odd feature in this appeal was that this argument about structure was accepted by the FTT in the context of the Section 103 Incumbrance Issue at FTT[214] to FTT[215] where the FTT referred to there being a "clear and obvious separation" between the disposition which created the incumbrance in s103(1) and the disposition of the property which was, or was represented by the property which was, the consideration for the creation of the incumbrance at s103(3). He submitted that the FTT did not fully explain why this structural issue did not apply where HMRC were relying on the "debt incurred", simply stating at FTT[235] "…although there is no need for there to be two dispositions of property in a case where Section 103 is being invoked by reference to the existence of a debt incurred (as opposed to being invoked by reference to the creation of an incumbrance), so that there isn't the same difficulty in squaring the language used in Section 103(3) with the language used in Section 103(1) to which we referred in paragraphs 214 and 215 above…". He submitted that this seems to have been based on the fact that "debt incurred by" does not include the word "disposition"; but that this is beside the point.

63. On the basis of the structure and language of s103, we agree with Mr Bradley that s103 envisages, and requires, two transactions – that which involved the creation of the liability consisting of a debt incurred by the deceased, and one in which any property was the subject matter of a disposition made by the deceased. The separation between these two transactions, which was identified by the FTT in the context of the Section 103 Incumbrance Issue, applies to liabilities consisting of debts incurred by the deceased as well as to incumbrances created by a disposition. This means that the Property, which was transferred by Mrs Elborne to the Life Settlement in consideration for the issue of the Note by the Life Trustees, cannot also be "property derived from the deceased" as defined by s103(3) for the purposes of s103(1)(a).

64. We did not find the decision in *McDougal's Trustees*, which was relied upon by HMRC, to be of any assistance. In that case, the deceased had bought recreational land which was conveyed, at his direction, by the sellers to the city authority of Edinburgh to hold as an open space. The money for the acquisition had been lent to him by that city authority, and the terms thereof were that the loan would not be called in until his death, at which time it was repayable with interest. The Inner House of the Court of Session (Lord Mackay dissenting) held that the loan and interest were not allowable deductions when computing the value of the deceased's estate.

65. The provision in issue in case was s31 FA 1939, the predecessor provision to s103, and, as with s103, provided that that the allowance for debts incurred by the deceased shall be subject to abatement to an extent proportionate to the value of any of the consideration given

therefor which consisted of "(a) property derived from the deceased; or (b) consideration not being such property as aforesaid, but given by any person who was at any time entitled to, or amongst whose resources there was at any time included, any property derived from the deceased". There was then a proviso to (b), which applied where it was proved that the value of the consideration given, or of that part thereof, exceeded that which could have been rendered available by application of all the property derived from the deceased, other than such (if any) of that property as is included in the consideration given; or as to which the like facts are proved in relation to the giving of the consideration as are mentioned in the proviso to s30(1), in which case no abatement shall be made in respect of the excess. The proviso to s30(1) provided for the exclusion from the property derived from the deceased any part thereof as to which it is proved that the disposition of which was not made with reference to, or with a view to enabling or facilitating, the purchase or provision of the annuity or other interest, or the recoupment of the cost thereof.

66. The Revenue had relied on s31(1)(b), and accepted that no part of the consideration given for the debt consisted of property derived from the deceased within s31(1)(a). The decision of the Court of Session thus addressed s31(1)(b) and the proviso thereto.

67. Both s31 and s103 include the alternative limbs (a) and (b), where (a) is "property derived from the deceased" and (b) is consideration not being property derived from the deceased. Given that the decision in *McDougal's Trustees* not only focuses on a different limb to that relied upon by HMRC in this appeal, but that limb is expressed to refer to consideration which is not property derived from the deceased, we have not, respectfully, found that decision to assist with the approach to be adopted to the interpretation of s103(1)(a).

68. Mr Davey drew our attention to the FTT's reference at FTT[235] to it being "very peculiar" if the application of s103 were to turn on the fact that the consideration given for the issue of the Note was provided simultaneously with, and not a scintilla of time before, the issue of the Note. He submitted that this would be an unattractive consequence of the Appellants' line of argument. However, s103(1) requires the identification of the consideration given for the relevant debt and we have concluded that it is a consequence of this, when considering the application of s103(1)(a), that prior dispositions of property by the deceased will be treated differently.

69. We therefore conclude that the FTT made an error of law when it concluded at FTT[235] that there is no need for there to be two dispositions of property in a case where s103 is being invoked by reference to the existence of a debt incurred and that the consideration for the Note consisted of property derived from Mrs Elborne for the purposes of s103(1).

**HMRC'S CROSS-APPEAL**

70. HMRC relied upon five alternative grounds in its cross-appeal.

(1) Three of the issues relied upon by HMRC, the Section 102 Property Issue, the Section 102A Issue and the Election Issue (the "Property Issues"), relate to the nature and/or value of Mrs Elborne's interest in the Property for inheritance tax purposes at the time of her death. These three issues have various distinct components (and the parties had mixed success on these components before the FTT) but each raise what we refer to as the "Section 102(3) Issue".

(2) The Section 49/*Rossendale* Issue and the Section 102 Note Issue, whilst being standalone grounds of cross-appeal, both relate to whether or not the value of Mrs Elborne's estate at the time of her death was depleted for inheritance tax purposes by an amount equal to the value of the Note.

**Property Issues**

71. HMRC's position was that the FTT's approach to and application of the decision in *St Barbe Green* was key to its decision on both the Section 103 Debt Incurred Issue and the Property Issues (as had been recognised by the FTT at FTT[120]) and that were the Upper Tribunal to disagree with the FTT on whether the Note was a debt incurred by Mrs Elborne, then that would undermine the FTT's decision in relation to the Property Issues (submitting this was acknowledged by the FTT at FTT[228]).

72. We set out the relevant legislation for all three of the Property Issues, address how the Section 102(3) Issue arises, the decision of the FTT, summarise the parties' submissions on the Section 102(3) Issue and then set out our discussion and conclusion.

73. The Section 102(3) Issue, which was decided by the FTT in favour of the Appellants, is not the only area of dispute between the parties on any of the three Property Issues. If we were to decide this issue in HMRC's favour, we would also need to address those further points of contention, and the varying circumstances in which the three issues could apply.

***Relevant Legislation***

74. Section 102 FA 1986 provides as follows:

> "102(1) Subject to subsections (5) and (6) below, this section applies where, on or after 18th March 1986, an individual disposes of any property by way of gift and either -
>
> (a) possession and enjoyment of the property is not bona fide assumed by the donee at or before the beginning of the relevant period; or
>
> (b) at any time in the relevant period the property is not enjoyed to the entire exclusion, or virtually to the entire exclusion, of the donor and of any benefit to him by contract or otherwise;
>
> and in this section "the relevant period" means a period ending on the date of the donor's death and beginning seven years before that date or, if it is later, on the date of the gift.
>
> (2) If and so long as -
>
> (a) possession and enjoyment of any property is not bona fide assumed as mentioned in subsection (1)(a) above, or
>
> (b) any property is not enjoyed as mentioned in subsection (1)(b) above,
>
> the property is referred to (in relation to the gift and the donor) as property subject to a reservation.
>
> (3) If, immediately before the death of the donor, there is any property which, in relation to him, is property subject to a reservation then, to the extent that the property would not, apart from this section, form part of the donor's estate immediately before his death, that property shall be treated for the purposes of the 1984 Act as property to which he was beneficially entitled immediately before his death.
>
> (4) If, at a time before the end of the relevant period, any property ceases to be property subject to a reservation, the donor shall be treated for the purposes of the 1984 Act as having at that time made a disposition of the property by a disposition which is a potentially exempt transfer….
>
> (8) Schedule 20 to this Act has effect for supplementing this section."

75. Paragraph 6 of Schedule 20 to the FA 1986 then provides that:

> "6(1) In determining whether any property which is disposed of by way of gift is enjoyed to the entire exclusion, or virtually to the entire exclusion, of the donor and of any benefit to him by contract or otherwise -
>
> (a) in the case of property which is an interest in land or a chattel, retention or assumption by the donor of actual occupation of the land or actual enjoyment of an incorporeal right over the land, or actual possession of the chattel shall be disregarded if it is for full consideration in money or money's worth;…
>
> (c) a benefit which the donor obtained by virtue of any associated operations (as defined in section 268 of the 1984 Act) of which the disposal by way of gift is one shall be treated as a benefit to him by contract or otherwise.
>
> (2) Any question whether any property comprised in a gift was at any time enjoyed to the entire exclusion, or virtually to the entire exclusion, of the donor and of any benefit to him shall (so far as that question depends upon the identity of the property) be determined by reference to the property which is at that time treated as property comprised in the gift..."

76. Section 268(1) defines associated operations as follows:

> "268(1) In this Act "associated operations" means, subject to subsection (2) below, any two or more operations of any kind, being -
>
> (a) operations which affect the same property, or one of which affects some property and the other or others of which affect property which represents, whether directly or indirectly, that property, or income arising from that property, or any property representing accumulations of any such income, or
>
> (b) any two operations of which one is effected with reference to the other, or with a view to enabling the other to be effected or facilitating its being effected, and any further operation having a like relation to any of those two, and so on,
>
> whether those operations are effected by the same person or different persons, and whether or not they are simultaneous; and "operation" includes an omission."

77. Section 84 and Schedule 15 FA 2004 introduced provisions which imposed a charge to income tax by reference to benefits received in certain circumstances by a former owner of property. These provisions are relevant to the Election Issue, where the key provisions in the present context are:

(1) paragraph 3 of the schedule, which provides for an individual who continues to occupy land after disposing of it to be liable to income tax on any amount by which the rental value of the land exceeds the payments made by the individual to the owner of the land in respect of his or her occupation of the land;

(2) paragraph 11(1) of the schedule, which provides that paragraph 3 of the schedule does not apply to a person when his or her estate for the purposes of inheritance tax includes the relevant property;

(3) paragraph 11(6) of the schedule, which provides that, where the value of the person's estate for inheritance tax is reduced by an excluded liability affecting any property, "that property is not to be treated for the purposes of [paragraph 11(1)]… as comprised in his estate except to the extent that the value of the property exceeds the amount of the excluded liability";

(4) paragraph 11(7) of the schedule, which provides that, for the purposes of paragraph 11(6) of the schedule, a liability is an "excluded liability" if, inter alia, the creation of the

liability and any transaction by virtue of which the person's estate came to include the relevant property were "associated operations", as defined in Section 268; and

(5) paragraph 21 of the schedule, which is headed "Election for application of inheritance tax provisions", and provides as follows:

> "21(1) This paragraph applies where -
>
> (a) a person ("the chargeable person") would (apart from this paragraph) be chargeable under paragraph 3 (land) or paragraph 6 (chattels) for any year of assessment ("the initial year") by reference to his enjoyment of any property ("the relevant property"), and
>
> (b) he has not been chargeable under the paragraph in question in respect of any previous year of assessment by reference to his enjoyment of the relevant property, or of any other property for which the relevant property has been substituted.
>
> (2) The chargeable person may elect in accordance with paragraph 23 that -
>
> (a) the preceding provisions of this Schedule shall not apply to him during the initial year and subsequent years of assessment by reference to his enjoyment of the relevant property or of any property which may be substituted for the relevant property, but
>
> (b) so long as the chargeable person continues to enjoy the relevant property or any property which is substituted for the relevant property –
>
> (i) the chargeable proportion of the property is to be treated for the purposes of Part 5 of the 1986 Act (in relation to the chargeable person) as property subject to a reservation, but only so far as the chargeable person is not beneficially entitled to an interest in possession in the property, ...
>
> (ii) section 102(3) and (4) of that Act shall apply, but only so far as the chargeable person is not beneficially entitled to an interest in possession in the property, and
>
> (iii) if the chargeable person is beneficially entitled to an interest in possession in the property, sections 53(3) and (4) and 54 of IHTA 1984 (which deal with cases of property reverting to the settlor etc) shall not apply in relation to the chargeable proportion of the property….
>
> (4) For the purposes of this paragraph a person "enjoys" property if –
>
> (a) in the case of an interest in land, he occupies the land, and
>
> (b) in the case of an interest in a chattel, he is in possession of, or has the use of, the chattel."

78. Section 102A FA 1986 provides as follows:

> "102A(1) This section applies where an individual disposes of an interest in land by way of gift on or after 9th March 1999.
>
> (2) At any time in the relevant period when the donor or his spouse or civil partner enjoys a significant right or interest, or is party to a significant arrangement, in relation to the land -
>
> (a) the interest disposed of is referred to (in relation to the gift and the donor) as property subject to a reservation; and
>
> (b) section 102(3) and (4) above shall apply.
>
> (3) Subject to subsections (4) and (5) below, a right, interest or arrangement in relation to land is significant for the purposes of subsection (2) above if

> (and only if) it entitles or enables the donor to occupy all or part of the land, or to enjoy some right in relation to all or part of the land, otherwise than for full consideration in money or money's worth.
>
> (4) A right, interest or arrangement is not significant for the purposes of subsection (2) above if -
>
> (a) it does not and cannot prevent the enjoyment of the land to the entire exclusion, or virtually to the entire exclusion, of the donor; or
>
> (b) it does not entitle or enable the donor to occupy all or part of the land immediately after the disposal, but would do so were it not for the interest disposed of.
>
> (5) A right or interest is not significant for the purposes of subsection (2) above if it was granted or acquired before the period of seven years ending with the date of the gift…."

***How the Section 102(3) Issue arises in the Property Issues***

79. Section 102 sets out (in s102(1) and (2)) the circumstances in which property disposed of is referred to as "property subject to a reservation". The consequence is then set out in s102(3), and this provides that where, immediately before the death of the donor, there is property subject to a reservation in relation to that donor, then "to the extent that the property would not, apart from this section, form part of the donor's estate immediately before his death, that property shall be treated for the purposes of the 1984 Act as property to which he was beneficially entitled immediately before his death".

80. The Section 102(3) Issue is thus whether the Property would otherwise form part of Mrs Elborne's estate immediately before her death for this purpose – if it would, then (subject to HMRC's submissions about the value in the estate) there can be no consequence for inheritance tax purposes even if the Property is "property subject to a reservation".

81. The Election Issue and the Section 102A Issue are then potentially relevant in different situations:

> (1) The making of an election treats the chargeable proportion of the property as property subject to a reservation, but only so far as the chargeable person is not beneficially entitled to an interest in possession in the property. HMRC submitted that the Election made by Mrs Elborne brings the part of the value of the Property which did not exceed the value of the liability under the Note within the estate. As made clear by Ms Belgrano, the Election Issue is relevant in the event that the Appellants succeed in the context of s102(1) on the disposal of the Property not being by way of gift.
>
> (2) Section 102A applies where an individual "disposes of an interest in land by way of gift" and may thus apply in circumstances where it has not been established that the requirements of s102(1) are met (albeit that both s102A(1) and s102(1) require that the relevant disposal is "by way of gift", a condition that Mr Bradley submitted was not met).

82. In both alternative situations, the consequence is then that s102(3) applies:

> (1) paragraph 21(2)(b)(ii) of Schedule 15 FA 2004 provides that (one consequence of) the election made by the chargeable person is that so long as the chargeable person continues to enjoy the relevant property then the chargeable proportion of the property is to be treated as property subject to a reservation and s102(3) applies (but only so far as the chargeable person is not beneficially entitled to an interest in possession in the property); and

(2) where s102A applies, the effect (as a result of s102A(2)) is to extend the application of s102(3) (and s102(4)) to the interest in land in question.

***Decision of the FTT***

83. The FTT had made observations about the decision in *St Barbe Green* at FTT[120] to FTT[128] (as we have summarised and addressed above), stating that this decision was significant to the Section 102 Property Issue as well as the Section 103 Debt Incurred Issue. These included the FTT having set out at FTT[127] that Mann J had referred to the settled property as being "property from which liabilities have been notionally deducted", then saying:

> "127. ...It therefore seems to us to be clear that the deduction of settlement liabilities is a matter which goes to calculating the value of the property to which the deceased is to be treated as being beneficially entitled as opposed to the identification of the property to which the deceased is to be treated as being beneficially entitled. We would add that further support for that proposition is to be derived from the terms of paragraph 11 of Schedule 15 to the FA 2004 because it is clear from the language in paragraph 11(6) of that schedule that a liability which affects the value at which property is to be brought into account in calculating the value of a person's estate does not prevent the part of the property which does not exceed that liability from being part of the estate. Otherwise, paragraph 11(6) would not have been needed."

84. In its discussion of the Section 102 Property Issue, the FTT accepted HMRC's submission that the preamble in s102(1) was satisfied in relation to the Property, concluding that there was a disposal of the Property by way of gift when Mrs Elborne sold the Property to the Life Trustees at an undervalue. It was common ground that the condition in s102(1)(b) was satisfied (and the FTT also concluded that the alternative condition in s102(1)(a) was satisfied).

85. The FTT's conclusion on the Section 102(3) Issue was therefore determinative in the Appellants' favour on the Section 102 Property Issue. The FTT explained its conclusion:

> "146. The short answer to the above submissions is that, in our view, Mr Bradley is right in saying that Section 102 can have no effect in relation to the Property because, for inheritance tax purposes, even before the application of the section, Mrs Elborne fell to be treated as beneficially entitled to the whole of the Property and therefore there is nothing to which Section 102(3) can apply. That is clear from the judgment of Mann J in St Barbe Green and it is supported by the way in which paragraphs 11(1), 11(6) and 11(7) of Schedule 15 to the FA 2004 are worded."

86. The FTT then identified (at FTT[163], FTT[181] and FTT[159]) that this conclusion essentially answered the Election Issue and the Section 102A Issue (but dealt with all of the matters contested between the parties in relation to those issues).

***Summary of parties' submissions***

87. Mr Davey, Ms Belgrano and Mr Bradley made submissions on all of the matters which would need to be decided in relation to the Property Issues (albeit that we indicated to HMRC at the hearing that we did not need to hear oral submissions from them in relation to the Section 102A Issue). We summarise only those submissions relevant to the Section 102(3) Issue.

88. HMRC's position was that if the Appellants were to persuade the Upper Tribunal to overturn the FTT's decision on the Section 103 Debt Incurred Issue and/or the FTT's application of *St Barbe Green* and thus the FTT's conclusion at FTT[237] that the liability under the Note constituted a debt deemed to be incurred by Mrs Elborne it would follow that, as the FTT put it, "the answer in relation to the Section 102 Property issue, the Section 102A

issue … would be very different" (FTT[228]). HMRC's position was that it was key to the FTT's conclusion on s102(3) that its analysis was that the Property did form part of the deceased's estate by virtue of s49(1) (and it was only the FTT's conclusion on this issue that caused HMRC to lose on the Section 102 Property Issue).

89. The FTT's conclusion in FTT[146] referred both to the decision in *St Barbe Green* and to the provisions of Schedule 15. At the hearing, Mr Davey addressed the former and Ms Belgrano the latter.

90. Mr Davey submitted that the FTT was referring at FTT[146] to the fact that on its analysis of s49(1) and the decision in *St Barbe Green*, the whole of the settled property, including the trust liabilities, is brought within the estate, therefore, when looking at this through the lens of s102(3), the Property would, apart from that section, form part of the estate immediately before death.

91. In HMRC's written submissions Mr Davey had submitted that if the initial step in that reasoning, ie that s49(1) treats the whole of the settled property as within the estate, is wrong, eg if s49(1) only brings a net value of the settled property into the estate, then that throws open the analysis in relation to s102(3), as the Property would not relevantly form part of Mrs Elborne's estate.

92. Mr Davey also submitted that if we were to agree with the FTT that s49(1) has the effect of bringing the Property within the estate, but disagree with the FTT's overall conclusion on the Section 103 Debt Incurred Issue, eg because we accept the Appellants' contention that the s49(1) deeming does not extend to treating Mrs Elborne as having incurred the liability under the Note, and/or that the s49(1) deeming does not apply for the purposes of considering s103, then HMRC's position was that the requirement that "the property would not, apart from this section, form part of the donor's estate immediately before his death" was still met. This is on the following basis:

> (1) The effect of property being subject to a reservation is that the entirety of the value of that property is brought into the donor's estate, which in turn reflects the policy of s102 FA 1986, as it was described in *Ingram v IRC* [2000] 1 AC 293 ("*Ingram*") at 305 namely "if the donor continued to derive any benefit from the property in which an interest had been given, it would be treated as a pretended gift unless the benefit could be shown to be referable to a specific proprietary interest which he had retained."
>
> (2) Hence, if the Property's value in the estate is, as on the Appellants' case, reduced to nil by virtue of the Note (ie reduced by virtue of a liability that was created solely in order to remove the value of the Property from Mrs Elborne's estate), then on a purposive reading of s102(3) the Property would not form part of Mrs Elborne's estate immediately before her death.

93. For this reason, HMRC did not agree with the Appellants' submission (which had been made in its written submissions) that if we agreed with the FTT that the Property was already part of Mrs Elborne's estate by virtue of s49(1) then this would be determinative of the Section 102(3) Issue.

94. Ms Belgrano dealt with the relevant provisions of Schedule 15, in particular paragraphs 11 and 21, in the context of her submissions on the Election Issue. Ms Belgrano submitted that whilst paragraph 11(6) provides that the relevant property was not to be treated as comprised in the relevant person's estate "for the purposes of sub-paragraph 11(1) or 11(2)", that deeming necessarily extended throughout Schedule 15, and should be applied for the purposes of paragraph 21. The consequence of this, Ms Belgrano submitted, was that paragraph 21(2)(b)(ii) applied to the Property to the extent of the value of the liability under the Note, and

therefore the Election had the effect of bringing the Property to that extent within the ambit of s102(3). Ms Belgrano submitted that the FTT's approach had deprived this deeming of proper effect.

95. Ms Belgrano then referred to the FTT's reasoning at FTT[146] where the FTT stated, without, she submitted, further explanation, that "That is clear from the judgment of Mann J in *St Barbe Green* and it is supported by the way in which paragraphs 11(1), 11(6) and 11(7) of Schedule 15 to the FA 2004 are worded". She submitted that, to the extent that the FTT had used these sub-paragraphs of paragraph 11 to construe earlier legislation in a different Act, that was an error of law. Ms Belgrano referred to *RFC 1012 plc v Advocate General for Scotland* [2017] UKSC 45 ("*Rangers*") and *Altrad Services Ltd v HMRC* [2024] EWCA Civ 720 ("*Altrad*") in support of this submission.

96. Mr Bradley submitted that the Property did form part of Mrs Elborne's estate for this purpose, submitting that this is exactly what s49(1) says. He submitted that the difficulty for HMRC was not whether the Property was in Mrs Elborne's estate but the value of the settled property that was taken into account. He submitted that s102(3) cannot assist HMRC in this regard – all it can do is put the Property back into the estate, but it was already there.

97. Responding to Ms Belgrano's submissions on paragraph 11(6), Mr Bradley submitted that paragraph 11(6) was intended to deal with the situation where property is within the estate but the value at which the property was brought into account was reduced by an excluded liability. He submitted that this argument "weakly supports" the FTT's conclusion in FTT[146], but that the FTT's decision was in any event based on its interpretation of s49(1) and *St Barbe Green*.

***Discussion on s102(3) Issue***

98. HMRC's position was that the FTT's decision on the Section 102(3) Issue involved an error of law, either on the basis that:

> (1) if we disagree with the FTT and conclude that s49(1) only brings a net value of the settled property into the estate rather than treating the whole of the settled property as within the estate, then that throws open the analysis in relation to s102(3), as the Property would not relevantly form part of Mrs Elborne's estate; or
>
> (2) if we were to agree with the FTT that s49(1) has the effect of bringing the Property within the estate, but disagree with the FTT's overall conclusion on the Section 103 Debt Incurred Issue, eg because we accept the Appellants' contention that the s49(1) deeming does not extend to treating Mrs Elborne as having incurred the liability under the Note, then HMRC's position was that the requirement that "the property would not, apart from this section, form part of the donor's estate immediately before his death" was met as the value of the Property would not be within the estate (as explained at [92] above).

99. The first alternative above was set out in HMRC's written submissions before the hearing, and it is this possibility that had been alluded to by the FTT at FTT[228] when it said that if Mann J was saying that the effect of s49(1) was that the deceased did not have an interest in possession in the portion of the gross settlement assets which did not exceed the liabilities then the answer on the Property Issues would be very different.

100. The Appellants did not advance any submissions in the context of the Section 103 Debt Incurred Issue that the FTT had made an error of law when it concluded at FTT[228] that Mann J was saying that the effect of the section was to confer on the holder of an interest in possession deemed beneficial ownership of the gross settlement assets but to take into account in valuing those assets the liabilities of the settlement. Mr Bradley expressly confirmed that the Appellants agreed with this part of the Decision, and HMRC supported the FTT's reasoning

on the Section 103 Debt Incurred Issue and thus did not advance any submissions that this was incorrect. Our decision on the Section 103 Debt Incurred Issued proceeded on this basis. We concluded that the deeming in s49(1) does not require the holder of the interest in possession to be treated as personally liable for the debts of the settlement. It is with this approach and conclusion in mind that we address the Section 102(3) Issue.

101. The question posed by s102(3) is whether there is any property (which is property subject to a reservation) that "would not, apart from this section, form part of [Mrs Elborne's] estate immediately before [her] death". We have already set out that s5(1) provides that "a person's estate is the aggregate of all the property to which he is beneficially entitled" and s49(1) then provides that for the purposes of IHTA 1984 a person beneficially entitled to an interest in possession in settled property "shall be treated …as beneficially entitled to the property in which the interest subsists". It was accepted by the parties that s49(1) brings the gross settlement assets within the estate and that the deduction of liabilities goes to calculating the value of the property, rather than the identification of the property to which the deceased is to be treated as being beneficially entitled. In this situation, we find Mr Bradley's submission that this is a complete answer to the Section 102(3) Issue compelling.

102. HMRC's submissions to the contrary were based on two alternative arguments:

(1) that where the Property's value in the death estate is reduced to nil by virtue of the Note then on a purposive reading of s102(3) the Property would not form part of Mrs Elborne's estate immediately before her death; and

(2) that the FTT erred in relying on paragraph 11 of Schedule 15 in support of its conclusion in FTT[146].

103. We reject both of those submissions, for the reasons which follow.

104. The statutory language, "to the extent that the property would not…form part of the donor's estate…", is clear, particularly when read alongside s5 and s49(1) which identify the property which is within the deceased's estate. Furthermore, there is no reference within s102(3) to whether there are liabilities which may be offset against the value of the relevant property or whether the result of the computation of the liability to inheritance tax is that tax is paid on the full value of the property. Here, the Property does form part of Mrs Elborne's estate immediately before her death by virtue of s49(1).

105. The FTT's reference to paragraph 11 in FTT[146] must be read in the light of the statutory context of paragraph 11 and the FTT's earlier statements in the context of its observations on *St Barbe Green*.

106. We have set out the statutory context of paragraph 11 above. Paragraph 11(6) provides:

> "11(6) Where at any time the value of a person's estate for the purposes of IHTA 1984 is reduced by an excluded liability affecting any property, that property is not to be treated for the purposes of sub-paragraph (1) or (2) as comprised in his estate except to the extent that the value of the property exceeds the amount of the excluded liability."

107. At FTT[127] the FTT stated:

> "127. …We would add that further support for that proposition is to be derived from the terms of paragraph 11 of Schedule 15 to the FA 2004 because it is clear from the language in paragraph 11(6) of that schedule that a liability which affects the value at which property is to be brought into account in calculating the value of a person's estate does not prevent the part of the property which does not exceed that liability from being part of the estate. Otherwise, paragraph 11(6) would not have been needed."

108. The FTT then reverted to this at FTT[146] where it said:

> "146. …That is clear from the judgment of Mann J in *St Barbe Green* and it is supported by the way in which paragraphs 11(1), 11(6) and 11(7) of Schedule 15 to the FA 2004 are worded."

109. The point being made by the FTT at FTT[146] had been amply explained in FTT[127].

110. Ms Belgrano submitted that the FTT made an error of law when relying on paragraph 11 when construing earlier legislation in a different Act. We disagree. Reading FTT[146] as a whole, we consider that the FTT's reference to paragraph 11 was immaterial to its decision. The FTT had said that its conclusion was "clear" from the judgment of *St Barbe Green*, a decision which it had carefully analysed. That was the reason for its decision. Furthermore, the authorities cited by Ms Belgrano in relation to using subsequent legislation to construe earlier legislation in a different Act do not support such a broad proposition.

111. In *Rangers*, Lord Hodge (with whom the remaining members of the Supreme Court agreed) said:

> "70. Part 7A of ITEPA was introduced by the Finance Act 2011 (section 26 and Schedule 2) and is designed to tax as employment income, among other things, the value of loans provided by third parties to employees under arrangements to reward employment. This legislation appears to have removed many of the benefits which some believed that the tax scheme gave. More recently, the Finance Act 2017 (section 15 and Schedule 6) has amended Part 7A of ITEPA. But these provisions, which are designed further to counter tax avoidance schemes, cannot affect the interpretation of prior tax legislation."

112. Lord Hodge was thus addressing the relevance (or otherwise) of the introduction and amendment of anti-avoidance provisions in Part 7A Income Tax (Earnings and Pensions) Act 2003 to the interpretation of the prior tax legislation on the meaning of employment income and earnings. There, Part 7A had been introduced to supplement what would otherwise be the meaning of employment income, with Lord Hodge having referred to Part 7A as having removed many of the anticipated benefits of the tax scheme, and the amendments being designed further to counter tax avoidance schemes.

113. In *Altrad*, Sir Launcelot Henderson (with whom the remaining members of the Court of Appeal agreed) said:

> "55. … In the course of its discussion of Issue 4, the UT pointed out at [46] that, when Parliament introduced remedial legislation in 2011 to 'correct the potential for anomalies' disclosed by schemes of the present type, it did so, in s 33 of the Finance Act 2011, by excluding from the calculation of both QE and QA any amount that could reasonably be assumed to constitute qualifying expenditure at the time when it was paid. Thus, if the taxpayers had implemented the same arrangements when s 33 was in force, on their analysis the arrangements would have produced no net benefit. There would instead have been a disposal value of 100 when the Assets were sold to the Bank, allowances of just 5 under the leaseback, no disposal value on termination of the lease, and qualifying expenditure of 95 under s 11 when the option price was paid. The UT also recorded the agreement of both parties that these later changes in the law cannot affect the true construction of the legislation as it stood when the taxpayers implemented their transactions: see again [46]. No doubt the parties were also in agreement that the enactment of such remedial legislation does not imply any recognition by the legislature that the scheme as implemented would have achieved its objective under the legislation then in force: that is the question for determination in the present proceedings."

114. Sir Launcelot Henderson thus confirmed that subsequent remedial legislation cannot affect the true construction of the earlier legislation.

115. Here, the provisions in issue are s102 and s49(1). Schedule 15 FA 2004 was introduced subsequent to these provisions, and was intended to sit alongside the earlier legislation – this is evident from the provisions of paragraph 21, which sets out the basis on which an election may be made in respect of other inheritance tax provisions. In this situation, the language of paragraph 11 may potentially be used to show how Parliament understood the existing legislation to operate. We put it no more strongly than that; and we do not consider that the FTT made an error of law when it referred to the wording of paragraph 11 in this situation.

116. The FTT's conclusion that s102 could not apply because Mrs Elborne fell to be treated as beneficially entitled to the whole of the Property and therefore there is nothing to which s102(3) can apply did not involve an error of law. This decision on the Section 102(3) Issue means that it is unnecessary for us to consider the further issues which would otherwise arise in relation to each of these three Property Issues and we do not do so.

117. HMRC's cross-appeals on the Section 102 Property Issue, the Election Issue and the Section 102A Issue are dismissed.

**Section 49/*Rossendale* Issue**

118. HMRC submit that the FTT erred in concluding that the liability under the Note should be taken into account by way of deduction for the purposes of s49. This is a logically prior argument to the Section 103 Debt Incurred Issue (and indeed to all of the issues based on s102 and s103). HMRC's position is that the liability was manufactured solely for the purpose of diminishing the value of the property in which Mrs Elborne's interest in possession subsisted and that, construing the legislation purposively and viewing the facts realistically, Parliament cannot be expected to have intended to exempt from the charge to inheritance tax a transaction which had no aim other than avoiding that charge to tax.

***Decision of the FTT***

119. The FTT stated it could see no basis in law for simply disregarding the liability under the Note in the light of its findings of fact to the effect that the parties to the Note intended it to have the legal effects which it purported to have and its conclusion of law to the effect that the Note gave rise to the legal effects which it purported to have (FTT[195]).

120. The FTT said it was not persuaded that the circumstances were akin to those in *Rossendale*:

> "197. …(1) in *Rossendale* at paragraph [51], Lord Briggs said expressly that the mere fact that a transaction is motivated by a tax avoidance purpose is not sufficient in and of itself to mean that the transaction can be disregarded. He said:
>
> "We emphasise that this conclusion is not founded on the fact that the defendant's only motive in granting the lease was to avoid paying business rates, although that was undoubtedly so. If the leases entered into by the defendants had the effect that they were not liable for business rates, their motive for granting the leases is irrelevant. Nor does it illuminate the legal issues to use words such as "artificial" or "contrived" to describe the leases, when it is now accepted that they created genuine legal rights and obligations and were not shams. Our conclusion is based squarely and solely on a purposive interpretation of the relevant statutory provisions and an analysis of the facts in the light of the provisions so construed";
>
> (2) it is therefore necessary in this context to ignore the tax avoidance motive which was underlying the scheme and focus instead on whether, on a

purposive construction of Section 49, as construed by Mann J in *St Barbe Green*, the liability under the Note falls outside the language in the section;

(3) we can see no basis for reaching that conclusion;

(4) in the first place, there is nothing in the language of Section 49 itself to support the proposition that the liabilities which are to be deducted in valuing the property which is subject to the interest in possession for the purposes of that section are to be disregarded in a case where they have been created for tax avoidance reasons;

(5) moreover, the scheme of the inheritance tax legislation as a whole is to make specific provision for those circumstances in which deductions for liabilities are to be disallowed because they have been incurred for tax avoidance reasons - for example, Sections 5(4) and 5(5), Section 162(5) of the IHTA and Section 103;

(6) we therefore infer that there is no reason why Section 49 should be construed on the basis that liabilities which have been incurred for tax avoidance purposes should be disregarded in applying that section and that this is not a case where a clear statutory purpose is being thwarted solely for tax avoidance reasons;

(7) we also see no relevance in this context in the fact that the liability under the Note was created at the same time as was the interest in possession or that the liability did not fall to be discharged in accordance with its terms until the interest in possession came to an end;

(8) as regards the first of those things, we can see no reason why the fact that the liability arose simultaneously with the creation of the interest in possession means that the liability falls to be disregarded in valuing that interest in possession and, as regards the second, we do not see why the fact that the liability could not fall due until after the interest in possession came to an end should cause the liability to be ignored. Clearly, the date on which a liability is due to be repaid and the obligations of the obligor pending that repayment will be matters which need to be taken into account in valuing the liability at the relevant time (see Section 162(2) of the IHTA). But they are not factors which go to the question of whether the liability should be taken into account at all; and

(9) we do not see any meaningful parallel between the facts in this case and the facts in *Montagu*… "

***Summary of parties' submissions***

121. Mr Davey submitted that the FTT erred in its interpretation of and approach to *Rossendale*.

122. Mr Davey submitted that the FTT had erred in underestimating the "acute potency" of the purposive construction which is required in the light of the recent and powerful statements in *Rossendale* and *Altrad*, drawing attention to:

(1) the explanation by the Supreme Court at [11] in *Rossendale* that the reason the result of applying a purposive approach to fiscal legislation has often been to disregard elements of transactions which have no business purpose and have as their sole aim the avoidance of tax is "because it is not generally to be expected that Parliament intends to exempt from tax a transaction which has no purpose other than tax avoidance"; and

(2) in *Altrad* Sir Launcelot Henderson had addressed *Rossendale* and the authorities cited therein and concluded at [40] "It seems to me that the Supreme Court here comes

close to enunciating a general principle which should be applied to the interpretation of all United Kingdom tax legislation…".

123. The Supreme Court in *Rossendale* had considered the operation of the ratings legislation and drawn a distinction between the "normal" situation and "unusual" circumstances, concluding that in the latter situation the person "entitled to possession" was not the person with the legal entitlement under the lease. Mr Davey submitted that the home loan scheme was "a transaction that does not appreciably affect [her] beneficial interest except to reduce [her] tax" (citing the oft-cited passage in *Gilbert v Commissioner of the Inland Revenue* [1957] 248 F 2d 399, which had been cited in both *Rossendale* and *Altrad*), and it is legitimate and necessary to keep in mind that Parliament cannot have intended that s49(1) was to be construed as providing passage for such an avoidance scheme. In a "normal" case, the person treated as beneficially entitled to property is treated as having incurred the trust liabilities; but in the unusual circumstances of this avoidance scheme, this should not include a liability such as the Note – it is one element of a scheme created solely to remove the value of the Property from the estate for inheritance tax purposes.

124. Mr Davey thus disagreed with the FTT's conclusion that one can't reach the conclusion that HMRC is contending for by a process of statutory construction, submitting that this underestimates the potency of the process which the *Ramsay* vein of authority, most recently articulated in *Rossendale*, entails.

125. Mr Bradley submitted that HMRC's approach was overly ambitious; *Rossendale* had emphatically confirmed that the *Ramsay* line of cases represented an application of general principles of statutory interpretation, and that there was no basis for being able to read s49 as contended by HMRC. He further submitted that it is not clear which words in s49(1) HMRC purport to be construing – it does not refer expressly to liabilities at all.

126. Mr Bradley also emphasised that HMRC's case on this issue necessarily depends on the factual allegation that the Life Trustees had no purpose in issuing the Note other than diminishing the value of the property in which Mrs Elborne's interest in possession subsisted. Ascertaining purpose involves an inquiry into the subjective intentions of the relevant actor; yet, as this allegation had not been made even in HMRC's amended statement of case, the Appellants had no opportunity to adduce evidence from Mr Woolfe (the sole surviving Life Trustee) as to his subjective intentions and accordingly it is too late for HMRC to pursue this allegation now.

***Discussion***

127. Mr Davey's submission was that the potency of the approach set out in *Rossendale* is such that not all trust liabilities are required to be taken into account when applying s49(1) and that, in particular, the liability of the Life Trustees under the Note should not be taken into account. Whilst Mr Davey emphasised that the transactions were part of a scheme, and the evidence of Mr Elborne (one of the Family Trustees but not a Life Trustee) had been that the sole purpose in implementing the scheme had been to remove the value of the Property from his mother's estate (FTT[18(1)]), it is clear from the approach of the Supreme Court in *Rossendale* that the principle is one of statutory interpretation and we should start our analysis with the relevant legislation.

128. We have set out s49(1) and its legislative context throughout this decision (including at [18] to [23], [58(2)] and [101]).

129. *Rossendale* concerned two schemes which had been entered into by the registered owners of various unoccupied commercial properties to seek to avoid liability for business rates. The

speech of Lord Briggs and Lord Leggatt (with whom Lord Reed, Lord Hodge and Lord Kitchin agreed) recorded at [5] that it was common ground that:

> (1) the schemes had no business or other "real world" purpose and that their sole purpose was to avoid liability to pay business rates, and
>
> (2) the leases granted to the SPVs were not shams so that, as a matter of the law of real property, they conferred an entitlement to possession upon the SPV.

130. Lord Briggs and Lord Leggatt repeatedly emphasised that the *Ramsay* principle is one of statutory interpretation, and at [15] reiterated that the task of ascertaining whether a particular statutory provision imposes a charge, or grants an exemption from a charge, involves two stages:

> "15. …The first [stage] is to ascertain the class of facts (which may or may not be transactions) intended to be affected by the charge or exemption. This is a process of interpretation of the statutory provision in the light of its purpose. The second is to discover whether the relevant facts fall within that class, in the sense that they "answer to the statutory description" (*Barclays Mercantile* at para 32). This may be described as a process of application of the statutory provision to the facts."

131. The went on at [16] and [17] to state that both of these stages share the need to avoid "tunnel vision" and stated that the facts must be looked at in the round.

132. In applying the law to the alleged facts of the test cases, their Lordships identified at [47] that in a "normal" case the "person entitled to possession" is the person who as a matter of the law of real property has the immediate legal right to actual physical possession of the relevant property. This accords with the legislative purpose of imposing the liability for business rates on the person who controls whether the property is left unoccupied and on whom the legislation is intended to place an incentive to bring the property back into use for the benefit of the community. However, in the "unusual" circumstances of this case, this would defeat the purpose of the legislation ([48]). The schemes were designed in such a way as to ensure that the SPV to whom a lease was granted had no real or practical control over whether the property was occupied or not, and that such control remained at all times with the landlord. Their Lordships then continued:

> "49. In our view, Parliament cannot sensibly be taken to have intended that "the person entitled to possession" of an unoccupied property on whom the liability for rates is imposed should encompass a company which has no real or practical ability to exercise its legal right to possession and on which that legal right has been conferred for no purpose other than the avoidance of liability for rates. Still less can Parliament rationally be taken to have intended that an entitlement created with the aim of acting unlawfully and abusing procedures provided by company and insolvency law should fall within the statutory description.
>
> 50. In these circumstances we have no difficulty in concluding that, on the agreed and assumed facts, the SPVs to which leases were granted as part of either of the schemes we have described did not thereby become "entitled to possession" of the demised property for the purposes of the 1988 Act. Rather, throughout the term of the lease that person remained the defendant landlord. This does not involve ignoring the leases, in the way that an intermediate element in a circular transaction might be ignored under the *Ramsay* doctrine. Rather it involves their close examination in their context, and a conclusion that they did not transfer to the SPVs the entitlement to possession required by the Act as the badge of ownership. If the defendants did not thereby transfer

> their entitlement to possession it necessarily remained, for the purposes of the Act, with them. The Act requires someone to be identified as the owner. That will be the person who, in any tenurial chain, starting with the freeholder and working downwards, has not disposed of the entitlement to possession of the property in question.
>
> 51. We emphasise that this conclusion is not founded on the fact that the defendant's only motive in granting the lease was to avoid paying business rates, although that was undoubtedly so. If the leases entered into by the defendants had the effect that they were not liable for business rates, their motive for granting the leases is irrelevant. Nor does it illuminate the legal issues to use words such as "artificial" or "contrived" to describe the leases, when it is now accepted that they created genuine legal rights and obligations and were not shams. Our conclusion is based squarely and solely on a purposive interpretation of the relevant statutory provisions and an analysis of the facts in the light of the provisions so construed."

133. Mr Elborne's evidence to the FTT included:

(1) the sole purpose in implementing the home loan scheme had been to remove the value of the Property from his mother's estate assuming that she was able to survive for more than seven years following the implementation of the scheme (FTT[18(1)]); and

(2) it was the intention of the parties at the time of implementing the scheme that the transaction documents would be adhered to (FTT[18(2)]).

134. That evidence appears to have been accepted by the FTT. The FTT found that despite the events which have occurred the parties involved in implementing the scheme intended to comply with the terms of the documents implementing the scheme at the time when the scheme documents were executed (FTT[26(1)]) and the true legal effect of the scheme documents was in accordance with their form and they gave rise to the rights and obligations set out in them (FTT[76]). A consequence of this is that the Note gave rise to a debt on the part of the Life Trustees and the Life Trustees still have an outstanding obligation to discharge the Note in accordance with its terms and the Family Trustees still have an entitlement to receive the proceeds of that discharge (FTT[78]).

135. We do not accept Mr Davey's submission that these facts represent an unusual case such that the liability represented by the Note should not be deducted when valuing the property to which Mrs Elborne is treated as beneficially entitled. The language and statutory context of s49(1) does not support this submission, and IHTA 1984 includes specific provisions for the disallowance of certain liabilities, eg s103. Moreover, whilst in *Rossendale* Lord Briggs and Lord Leggatt referred to the SPVs as having no real or practical ability to exercise their legal right to possession, and to that legal right having been conferred for no purpose other than the avoidance of liability for rates, in the present case the FTT made findings as to the Note giving rise to a debt and there was no finding as to the purpose of the Life Trustees in issuing the Note on its particular terms.

136. The FTT had referenced its "strong suspicion" (at FTT[79]) that had Mrs Elborne died within seven years of making the gift of the Note then HMRC would have sought to claim that that gift had inheritance tax consequences, thereby recognising the validity of the Note. Whilst we do not place any weight on this, we do recognise that this was also Mr Elborne's expectation (based on his evidence at FTT[18(1)]).

137. The FTT's decision on the Section 49/*Rossendale* Issue did not involve an error of law and HMRC's cross-appeal on this issue is dismissed.

**Section 102 Note Issue**

138. HMRC submit that s102 applies in respect of the transfer by Mrs Elborne of her interest in the Note with the effect that such interest falls to be treated as property to which Mrs Elborne was beneficially entitled immediately before her death and forms part of the value transferred by way of the deemed transfer of value immediately before her death.

139. There are five components that must be satisfied for the Note to fall within s102:

(1) there is an individual;

(2) that individual disposes of property;

(3) that disposal is by way of gift;

(4) the position is such that the case comes within s102(1)(a) or 102(1)(b); and

(5) the requirements of s102(3) are met, ie the property would not otherwise form part of the donor's estate immediately prior to death.

140. It was common ground that the requirements of (1), (2), (3) and (5) were satisfied in relation to the Note. The issue is whether the requirements of s102(1)(a) or s102(1)(b) are met, ie whether:

> "(a) possession and enjoyment of the property is not bona fide assumed by the donee at or before the beginning of the relevant period; or
>
> (b) at any time in the relevant period the property is not enjoyed to the entire exclusion, or virtually to the entire exclusion, of the donor and of any benefit to him by contract or otherwise;
>
> and in relation to this section "the relevant period" means a period ending on the date of the donor's death and beginning seven years before that date or, if it is later, on the date of the gift"

141. Not only are s102(1)(a) and s102(1)(b) alternative requirements, but s102(1)(b) has two (alternative) limbs. The first limb applies if gifted property is not enjoyed to the entire exclusion, or virtually to the entire exclusion, of the donor. The second limb applies if gifted property is not enjoyed to the entire exclusion, or virtually to the entire exclusion, of any benefit to the donor by contract or otherwise. Whilst HMRC's submissions mainly addressed the second limb of s102(1)(b), they relied in the alternative on s102(1)(a) or the first limb of s102(1)(b) applying.

***Decision of the FTT***

142. The FTT's conclusion on the first limb of s102(1)(b) was as follows:

> "256. …the starting point must be to observe that there can be no dispute in this case about the subject matter of the gift – namely, the Note – or over whether, following the gift of the Note, the Note itself was enjoyed to the exclusion, or virtually to the entire exclusion, of Mrs Elborne. That is because, following the gift, Mrs Elborne had no further interest in the Note as she was precluded from benefiting from it under the terms of the Family Settlement. That means that the first limb of the condition in Section 102(1)(b) cannot apply in relation to the gift of the Note…"

143. The FTT then addressed the second limb of s102(1)(b), and concluded that the authorities show that the following three conditions must be satisfied:

> "257. …(1) Mrs Elborne must have enjoyed a benefit in the relevant period, which is to say, a period which, by definition, commences after the making of the gift. If no benefit was enjoyed in the "relevant period", then the second

limb of the test in Section 102(1)(b) cannot be satisfied in relation to the Note because that is what the provision requires;

(2) if Mrs Elborne did enjoy a benefit in the relevant period, the benefit must have consisted of some advantage which Mrs Elborne did not enjoy before the gift was made and before any of the "associated operations" in relation to the gift occurred. If the benefit consisted of an advantage that Mrs Elborne enjoyed before the gift was made and before any of the "associated operations" in relation to the gift occurred, then the second limb of the test in Section 102(1)(b) cannot be satisfied in relation to the Note - see *Hood* at paragraphs [42] to [44], [60] and [65]; and

(3) if the benefit did consist of an advantage that Mrs Elborne did not enjoy before the gift was made or before any of the "associated operations" in relation to the gift occurred, that benefit must have impacted upon the enjoyment by the trustees of the Family Settlement of the gifted asset - namely the Note. If the benefit did not impact upon, or "trench upon", the enjoyment by the trustees of the gifted asset, then the second limb of the test in Section 102(1)(b) cannot be satisfied in relation to the Note - see *Buzzoni* at paragraphs [50] to [57] and *Hood* at paragraphs [51], [52] and [65]."

144. The FTT identified the benefit to Mrs Elborne and concluded that whilst the first condition was met the second and third were not:

"258. Turning to the application of the above conditions in the present case, the first condition is clearly satisfied by virtue of the benefit to Mrs Elborne of being able to occupy the Property following the gift of the Note. That was a benefit to Mrs Elborne by contract or otherwise for the purposes of Section 102(1)(b) because, regardless of whether it arose by virtue of the terms of the Note itself (as Mr Davey submitted), it certainly arose by virtue of one or more of the transactions which were "associated operations" in relation to the gift of the Note such as the agreement to transfer the Property to a settlement under which Mrs Elborne enjoyed an interest in possession or the terms of the Life Settlement Trustees' Resolution.

259. However, that benefit was something which Mrs Elborne enjoyed before she made the gift of the Note to the trustees of the Family Settlement and indeed before the scheme commenced and the chain of "associated operations" in relation to the gift started. That benefit was not something which arose for the first time as a result of either the gift or any of the "associated operations" in relation to the gift and consequently we consider that the condition set out in paragraph 257(2) above is not met.

260. Moreover, as regards the condition set out in paragraph 257(3) above, the benefit was not one which "trenched upon" the enjoyment of the Note by the trustees. The fact that the trustees were unable to require the Note to be repaid, absent a default, until Mrs Elborne had died was not something which "trenched upon" their enjoyment of the Note because those terms were simply an integral part of the gifted property. Whilst the decisions in *Buzzoni* and *Hood* demonstrate that a benefit which arises as a result of a term in the gifted property is not precluded from being a relevant benefit for the purposes of Section 102, that is true only of a term which is created as part of the gift itself. It is not true of a contractual provision which pre-dates the gift because an advantage enjoyed both before and after the gift is made can hardly be a reservation out of the gift - see *Buzzoni* at paragraph [51] and *Hood* at paragraphs [60] and [65]."

145. The FTT then addressed the alternative requirement in s102(1)(a), concluding that the Family Trustees had assumed relevant possession and enjoyment of the Note. The FTT referred to its analysis in [260] and stated:

> "261. …The trustees of the Family Settlement may have been precluded, absent a default, from demanding repayment of the Note until Mrs Elborne died, but that was a function of the terms of the Note – which is to say the terms of the gifted property. It has no effect on the ability of the trustees to possess and enjoy the gifted property."

***Summary of parties' submissions***

146. HMRC's position was that the FTT had erred in law in concluding that none of s102(1)(a) or the first or second limb of s102(1)(b) applied. The majority of Mr Davey's submissions were made by reference to the FTT's approach to the second limb of s102(1)(b), but he relied on a similar approach in the context of the alternative paragraphs.

147. Mr Davey submitted that when applying s102 to the present facts, it was crucial to recognise that the transactions entered into were part of a scheme - a composite set of arrangements - and then to view them as a unity, submitting that the statutory extension to benefits obtained by virtue of any "associated operations" reflected this approach. In their written submissions HMRC stated that the FTT had correctly identified this benefit, albeit they had then stated that the FTT had erred in how it then analysed this. In his oral submissions, Mr Davey submitted that the FTT had erred in defining benefit narrowly as Mrs Elborne's ability to occupy the Property. The terms of the Note were that it would not be repaid, absent a default, until Mrs Elborne died. This meant that the Life Trustees would not have to sell the Property to raise funds to repay the Note, so Mrs Elborne could continue to live at the Property. The benefit to Mrs Elborne was thus inseparable from the gifted property.

148. Mr Davey submitted that having found that Mrs Elborne "clearly" enjoyed a benefit in the relevant period by virtue of being able to occupy the Property following the gift of the Note, and that this benefit arose by virtue of one of more of the transactions which were "associated operations" in relation to the gift of the Note (at FTT[258]), the FTT should then have concluded that the Note was "property subject to a reservation" for the purposes of s102(2).

149. It was HMRC's position that the FTT had erred in law in reaching its conclusion on the second limb of s102(1)(b). Mr Davey submitted that:

(1) the FTT erred in holding that the benefit to Mrs Elborne relevantly pre-dated the gift and the associated operations (at FTT[257(2)] and FTT[259]) - the FTT erred in identifying the benefit (which it had described as being able to occupy the Property following the gift of the Note) as something she enjoyed before the gift – she had previously lived in the Property as owner of the freehold, whereas after the scheme she did so in her capacity of the holder of the interest in possession of the Life Settlement. The FTT failed properly to factor in the impact of paragraph 6 of Schedule 20; the test there is a causal one, "a benefit which the donor obtained by virtue of any associated operations"; and

(2) the FTT erred by imposing a trenching requirement which is absent from the legislation (at FTT[257(3)] and FTT[260]). Further, if and to the extent there is such a requirement, the inability of the Family Trustees to require repayment of the Note prior to Mrs Elborne's death did encroach or trench upon their rights as donees.

150. Mr Davey submitted in the alternative that the FTT erred in holding at FTT[256] that s102(1)(b) could not apply to the Note itself and that the first limb of s102(1)(b) was not met. He submitted that Mrs Elborne reserved a benefit from the Note because the terms of the Note,

coupled with her life interest in the Life Settlement, ensured that the liability which the Note represented could not be required to be repaid prior to her death and that she would, after the scheme, have the right to reside at the Property until her death.

151. In the further alternative, Mr Davey submitted that possession and enjoyment of the Note was not bona fide assumed by the Family Trustees during Mrs Elborne's lifetime for the purposes of s102(1)(a) because there was no possibility of the Note being repaid until after her death, and the Note was not turned into account, or intended to be turned into account, in any other way. The FTT's imposition of a trenching requirement at FTT[260] and FTT[261] was erroneous in this context (for the same reasons as relied upon in the context of s102(1)(b)).

152. Mr Bradley cautioned against taking a broad brush approach on the basis that the transactions involved a scheme, pointing out that the facts in *Ingram* and *Buzzoni and others v HMRC* [2013] EWCA Civ 1684 ("*Buzzoni*") had also involved schemes to remove the value of property from the estate yet enabling the donor to continue to occupy the property.

153. Mr Bradley submitted that the requirements of s102(1)(b) were not met. He submitted that the benefit must be referable to the property that was given away, relying on Lord Hoffmann's speech in *Ingram* where, having described the theme running through the cases as being that although s102 does not allow a donor to have his cake and eat it, there is nothing to stop him from carefully dividing up the cake, eating part and having the rest, Lord Hoffmann had then cited *St. Aubyn v Attorney General* [1952] AC 15 ("*St. Aubyn*") at 22-23 for the proposition that if the benefit which the donor continues to enjoy is by virtue of property which was never comprised in the gift, he has not reserved any benefit out of the property of which he disposed.

154. Mr Bradley submitted that the FTT had not erred in holding that the benefit must be one that did not exist before the gift and the benefit must be one that negatively impacts, or trenches upon, the donee's enjoyment of the gifted property. He submitted that intuitively there is something odd about HMRC's case which seeks to establish that there had been a reservation of benefit in the gifted property, the Note, because of something that Mrs Elborne enjoyed in relation to the Property. Mr Bradley drew attention to the timing of the various transactions, including that whilst Mrs Elborne had initially occupied the Property as owner of the freehold, she had then occupied by virtue of her life interest in the Life Settlement before assigning the Note to the Family Trustees.

155. Mr Bradley submitted that we must look at the words of the statute, which are compound phrases and have been heavily interpreted. He submitted that we are bound by the decision of the Court of Appeal in *Buzzoni* in relation to both of the conclusions relied upon by the FTT in reaching its decision.

156. Addressing HMRC's case on s102(1)(a), Mr Bradley submitted that the Family Trustees had assumed bona fide possession and enjoyment of the Note; it was irrelevant that the terms of the Note were such that, absent an event of default, the Note was not repayable until after Mrs Elborne's death.

***Discussion***

157. The FTT had concluded that requirements of s102(1)(a) and s102(1)(b) were not met. HMRC submits that the FTT erred in reaching these conclusions.

*Section 102(1)(b) – exclusion of any benefit to the donor (second limb)*

158. We address first the second limb of s102(1)(b) which applies if "at any time in the relevant period the property is not enjoyed to the entire exclusion, or virtually to the entire exclusion, ... of any benefit to [the donor] by contract or otherwise". This must be read in

conjunction with paragraph 6 of Schedule 20. Paragraph 6(1)(c) provides that in determining whether gifted property is subject to a "benefit" to the donor by contract or otherwise:

> "a benefit which the donor obtained by virtue of any associated operations (as defined in section 268 of the 1984 Act) of which the disposal by way of gift is one shall be treated as a benefit to him by contract or otherwise."

159. It was common ground that all of the steps involved in the home loan scheme are "associated operations" for this purpose.

160. Mr Davey submitted that the FTT had erred in effectively elevating factors which had been helpful in analysing other fact-patterns into statutory requirements, and that the FTT had taken too narrow an approach to identifying the benefit to Mrs Elborne.

161. Mr Davey and Mr Bradley each took us to the leading authorities, including the decisions of the Court of Appeal in *Buzzoni* and *Viscount Hood v HMRC* [2018] EWCA Civ 2405 ("*Hood*") in support of their respective submissions.

162. The most recent authorities on s102 all involved the creation of various legal interests in an asset, a house, in which the donor continued to reside after giving away a legal interest in that asset. As identified by Lord Hoffmann in *Ingram*, the theme which runs through the cases is that although s102 does not allow a donor to have his cake and eat it, there is nothing to stop him from carefully dividing up the cake, eating part and having the rest. If the benefits which the donor continues to enjoy are by virtue of property which was never comprised in the gift, he has not reserved any benefit out of the property of which he disposed. Lord Hoffmann reiterated this later in his speech, having set out the policy of s102, explaining that "property" in s102 is not something which has physical existence, but a specific interest in that property, a legal construct, which can co-exist with other interests in the same physical object.

163. The policy of s102 and the theme identified by Lord Hoffmann help to explain why s102 may be found not to apply to a given set of facts; but it does not obviate the need to analyse and apply the statutory language.

164. In *Buzzoni*, the deceased, a lessee under a head lease, granted a rent-free underlease to a nominee of the trustee of a settlement for her sons, retaining the reversion to the underlease. The deceased had covenanted with the head lessor in the head lease not to underlet the property, unless the underlessee first entered into a covenant with the head lessor to observe certain of the tenant's covenants and obligations contained in the head lease. By a licence to underlet (the "licence"), the head lessor gave consent to underlet and the underlessee covenanted directly with the head lessor to observe and perform the tenant's covenants and conditions (other than payment of rent) contained in the head lease. The deceased then granted the underlease, which contained positive covenants under which the underlessee covenanted to observe the covenants to which the underlessor was subject under the head lease.

165. The issue was whether the underlease had been enjoyed by the donee "to the entire exclusion of the donor or any benefit to [her] by contract or otherwise" within the meaning of the second limb of s102(1)(b). It was agreed that the benefit of the positive covenants in the underlease was a benefit for the deceased.

166. HMRC submitted that the positive covenants in the underlease constituted a benefit taken by the deceased back from the property she gave and that, therefore, the donees did not enjoy the underlease to the exclusion of a benefit to the donor. HMRC submitted that this was the only issue, and that the court had to decide the source of the positive covenants from which the deceased benefitted, namely whether they were received back from the underlease of which she disposed (ie referable to the property gifted), or benefits enjoyed by virtue of her reversionary interest in the head lease which was never comprised in the gift.

167. The taxpayers submitted that even if the source of the positive covenants was the underlease, this was not sufficient for 102(1)(b) to apply; it was necessary also to show that the benefit affected the enjoyment by the donee of the property gifted, not enjoyment by the donor of the benefit. The taxpayer's contention was that the impugned benefit made no difference to the donee's enjoyment of the underlease as the covenants mirrored the covenants which the donee had already given to the head lessor under the licence.

168. The Court of Appeal allowed the taxpayers' appeal. The leading judgment was given by Moses LJ.

169. Moses LJ first addressed the source of the benefit. This was, according to HMRC, the only question ([17]). The deceased had created two separate interests in the head lease, the reversion and the underlease, and made a gift only of the underlease. It was not suggested, nor could it be, that the reversion was itself a reservation out of the subject-matter of the gift ([18]). The deceased had obtained positive covenants, and the first question was whether it can be said that those positive covenants should be regarded as rights which the deceased enjoyed by virtue of her reversionary interest which was never comprised in the gift, or whether they were enjoyed by virtue of the underlease, of which she did make a gift ([22]). Apart from the positive covenants, she had no right to impose a liability on the underlessees to keep the flat properly decorated and to redecorate every fifth year ([27]). The sequence of events, which had involved first the entry into the licence (in which the nominee for the taxpayer trustee covenanted with the head landlord to observe the tenant's covenants in the head lease, before the underlease was subsequently settled on the taxpayer trustee), did not make any difference ([28] to [29]). Looking at the reality, the covenants conferred rights on the deceased which arose from the obligations imposed in the underlease. The rights conferred by the covenants were obtained by virtue of the underlease, the subject of the gift, and not by virtue of the reversion the deceased retained ([29]).

170. Moses LJ then addressed the parties' submissions in relation to the impact on the exclusivity of the donees' enjoyment. HMRC's submission was that the conclusion as to the source of the benefit was dispositive.

171. Moses LJ referred to various authorities, including *St. Aubyn*, *Ingram*, *Earl Grey v Attorney General* [1900] AC 124, and *Chick v Commissioner of Stamp Duties* [1958] AC 435. Moses LJ concluded that the authorities did not "carry the taxpayers as far as they need to go". They do show that it may not be sufficient to ask whether the donor has received a benefit, but none of them turn on any further inquiry as to whether, even if it was derived from the gifted property, the benefit was at the cost or expense or to the detriment of the donee's enjoyment ([49]).

172. Instead, Moses LJ accepted the taxpayers' submission based on the wording of the legislation:

> "50. It seems to me that there is sufficient support for the taxpayers' contention to be found in the wording of the subsection. The second limb of section 102(1)b) requires consideration of whether the donee's enjoyment of the property gifted is to the exclusion of any benefit to the donor. The focus is not primarily on the question whether the donor has obtained a benefit from the gifted property, but whether the donee's enjoyment of that property remains exclusive. The statutory question is whether the donee enjoyed the property to the entire exclusion or virtually to the entire exclusion of any benefit to the donor. If the benefit to the donor does not have any impact on the donee's enjoyment, in my view, then the donee's enjoyment is to the entire exclusion of any benefit to the donor.

> 51. Millet LJ said that to come within the scope of the second limb of the subsection the benefit must consist of some advantage which the donor did not enjoy before he made the gift. That was sufficient in *In re Nichols, decd* [1975] 1 WLR 534 and would have been in *Ingram's case* [2000] 1 AC 293 where any such advantage clearly would have had an impact on the subject matter of the gift. But whilst that is a necessary condition, there will be cases in which it is not a sufficient condition. As I have said, the subject, in its focus on the exclusivity of the donee's enjoyment of the gifted property, may demand further inquiry as to whether the benefit has any impact upon the donee's enjoyment. If the benefit is irrelevant to such enjoyment it does not "trench upon" the exclusivity of the donee's enjoyment."

173. Moses LJ referred to the policy of s102, citing at [53] Lord Hoffman's summary of that policy at p304-305 in *Ingram*:

> "53. …(section 102) … is in one sense a penal section. Not only may you not have your cake and eat it, but if you eat more than a few de minimis crumbs of what was given, you are deemed for tax purposes to have eaten the lot … What, then, is the policy of section 102? It requires people to define precisely the interests which they are giving away and the interests, if any, which they are retaining. Once they have given away an interest they may not receive back any benefits from that interest. In *Lang v Webb* (1912) 12 CLR 503, 513 Isaacs J suggested that the policy was to avoid the "delay, expense and uncertainty" of requiring the revenue to investigate whether a gift was genuine or pretended. It laid down a rule that if the donor continued to derive any benefit from the property in which an interest had been given it would be treated as a pretended gift unless the benefit could be shown to be referable to a specific proprietary interest which he had retained. This is probably the most plausible explanation and accepting this as the policy, I think there can be no doubt that the interest retained by Lady Ingram was a proprietary interest defined with the necessary precision."

174. Moses LJ concluded that the benefit to the deceased obtained from the positive covenants "made no difference whatsoever" to the underlessees' enjoyment of the underlease. They were already under obligations, in the licence, to the head lessor which precisely matched those obligations. Even if the deceased obtained a benefit she had not previously enjoyed, it was not obtained at the expense of the donees' enjoyment of the underlease ([56]).

175. Black LJ and Gloster LJ agreed that the appeal should be allowed, and both specifically said that this was for the reasons given by Moses LJ from [30]. They both said it was therefore not necessary for them to decide the question whether the benefit of the positive covenants in the underlease derived from the interest retained by the deceased when she made the gift or from the property which she had gifted and they did not do so (at [58] and [59] respectively).

176. *Hood* is a later decision of the Court of Appeal. Its facts bore some "generic similarity" to those in *Buzzoni*, but with "one significant difference which eventually won the day for the taxpayers" (Henderson LJ at [45]). The deceased held a head lease in a property and entered into a reversionary sub-lease with her sons on favourable terms for the residue of the term granted by the head lease, less three days. The sub-lease contained covenants under which the sub-lessees agreed to observe and perform the provisions in the head lease as if those provisions had been repeated in full in the sub-lease. The issue was whether the requirements of the second limb of s102(1)(b) were satisfied.

177. HMRC submitted that the sons' enjoyment of the sub-lease was not "to the entire exclusion, or virtually to the entire exclusion, ... of any benefit [to the donor] by contract or otherwise". This was because the sons entered into the direct covenant with their mother in

the sub-lease to perform the obligations; and the benefit of this covenant was a benefit by contract to the taxpayer which had no prior existence before the sub-lease was granted, and which was of substantial value to her.

178. The taxpayer submitted that the court needed to "identify with precision" the donated property. He submitted that the covenants in the sub-lease formed an integral part of the gift and cannot be divorced from it; the subject-matter of the gift had these covenants "imprinted" upon it – they were part and parcel of the gift itself.

179. Henderson LJ gave the leading judgment (with which Sir Colin Rimer and Patten LJ agreed). Henderson LJ noted that the decision in *Ingram* had turned on the first limb of s102(1)(b), but the judgments of Millett LJ (dissenting in the Court of Appeal) and Lord Hoffmann had thrown helpful light on the second limb ([41]). Millett LJ had observed that it was clearly established that it was not necessary for the benefit to the donor to be reserved out of the subject-matter of the gift, but "the benefit must consists of some advantage which the donor did not enjoy before he made the gift, and that it is not sufficient if it consists merely of the property which he owned before the gift and which was not included in it". The landlord's covenant for quiet enjoyment could not be separated from the lessee's right of exclusive possession in that case ([42]). Lord Hoffmann's reasoning was that, where a leasehold estate is created, whether by way of gift of by way of reservation upon a transfer of the reversion, there will be a reservation of benefit if the donor received the benefit of contractual benefits which had no prior existence ([44]).

180. At [52] Henderson LJ determined that the outcome in *Buzzoni* had turned on the fact that the underlessees had already entered into direct covenants with the head lessor to observe and perform the covenants in the head lease before the underlease was granted.

181. Henderson LJ accepted that it was necessary to begin by identifying the true subject matter of the gift made by the deceased, as that is the "property" to which s102 had to be applied ([59]). The estate in land and the covenants formed part of a single transaction, and it would be artificial to distinguish between them because neither would have come into existence without the other. He described the gift as being of an interest in land subject to, and with the benefit of, the obligations which the parties agreed to undertake in the sub-lease.

182. Henderson LJ then explained:

> "60. Where I respectfully part company from Mr Taube, however, is when he goes on to submit that this identification of the subject matter of the gift is sufficient to exclude the operation of section 102. In my judgment, it is necessary to pay close attention to the wording of section 102(1)(b), and in particular to its second limb. The property, that is to say the sub-lease viewed as a whole, will be property subject to a reservation in Lady Hood's estate unless it was enjoyed by the donee, that is to say her sons, to the entire exclusion, or virtually to the entire exclusion, of any benefit to her by contract or otherwise. How, I ask, can this condition be satisfied, when Lady Hood, in her capacity as the intermediate or mesne lessor of the Property, now had the benefit of the positive covenants given by her sons, including the obligation to observe and perform the provisions of the head lease throughout the term of the sub-lease? True, those benefits were future ones, in the sense that they would only come into force when the sub-lease fell into possession in March 2012; but they would then enure for the benefit of Lady Hood (or her estate after her death) until 2076 or the prior termination of either the head lease or the sub-lease. This was undoubtedly a benefit to Lady Hood of real, and more than minimal, value; and, crucially, it had no prior existence before the grant of the sub-lease. How, then, can it be said that the grant of the sub-lease did not involve the reservation by Lady Hood of a benefit by way of contract?

> 61. In my view, it is no answer to this question to say that the positive covenants which give rise to the benefit formed an integral part of the original gift. So they did, but that is a separate question from whether the enjoyment of the gift by the sons (and their successors entitled to the sub-lease) was free of any benefit to the donor. On the facts of a case such as this or *Buzzoni*, the benefit to the donor was inseparable from the gift, but that only goes to show the closeness of the connection between the gift and the benefit. Incidentally, it also obviates the need for any separate enquiry as to whether the benefit was referable to, or trenched upon, the gift, because (as I have said) one could not have existed without the other. Indeed, the connection could hardly have been closer.
>
> 62. The fact that the sons' covenants had no prior existence is in my judgment of critical importance for at least two reasons. First, it leaves little, if any, room for an argument that the benefit was something retained by the donor, or otherwise separate from the gift which she made. Rather, the benefit was an inherent part of the gift itself. Secondly, it distinguishes cases of the present type from ones such as *Ingram* or *St Aubyn*, where the donor takes advantage of the sophisticated nature of English land or trust law so as to define the property given away in such a manner that any benefits retained by the donor never formed part of the gift at all."

183. Henderson LJ went onto to agree that the Court of Appeal in *Nichols* was right to emphasise that the donor's right to have the mansion house and outbuildings repaired under the covenant did not exist before and therefore could not be something simply not given. Similarly, he agreed with Millett LJ in *Ingram* that the benefits must consist of some advantage which the donor did not enjoy before he made the gift ([63]).

184. At [65] Henderson LJ stated that he agreed with the reasoning of Moses LJ in *Buzzoni* at [51] that the benefit must consist of some advantage which the donor did not enjoy before he made the gift, and observed that this part of Moses LJ's judgment carried the agreement of both Black and Gloster LJJ and "at least arguably" forms part of the ratio of the decision. The further enquiry in that case as to whether the benefit has any impact upon the donee's enjoyment was answered in the taxpayers' favour, but no similar argument could be mounted here, as the sons had not entered into separate covenants with the head lessor in the licence to underlet.

185. Mr Davey's submissions were focused on the FTT's reasoning at FTT[257] to FTT[260], in particular the FTT's identification of the benefit, the timing of that benefit and whether it is a requirement that the benefit trench upon the donee's enjoyment of the gifted property (and, if so, whether this was met). Mr Bradley supported the reasoning of the FTT, and also submitted that the Note was not property subject to a reservation within s102 as any benefit to Mrs Elborne was not referable to the property that was given away.

186. The FTT identified the benefit to Mrs Elborne as that of being able to occupy the Property following the gift of the Note. Whilst HMRC's approach differed between its written and oral submissions, it was nevertheless clear at the hearing that Mr Davey's submission was that the benefit to Mrs Elborne of the ability to occupy the Property needed to be analysed in the context of the gift of the Note and the associated operations, and that the benefit arose by virtue of the gift and those operations, which included the terms of the Note in relation to repayment, namely that it was not repayable by the Life Trustees until after Mrs Elborne's death. Mr Davey relied in particular on the decision in *Hood*, submitting that the benefit to Mrs Elborne and the gifted property, the Note, were inseparable; he submitted that the FTT fell into error when it held that it made a material difference that Mrs Elborne was able to occupy the Property before she made a gift of the Note.

187. On the facts here, we agree not only with the FTT's description of the benefit being Mrs Elborne's ability to occupy the Property but also that this benefit arose by virtue of one or more of the transactions which were associated operations for this purpose. That it arose in this way does not, however, mean that it was an integral part of the gift or inseparable from the gifted property, the Note. Mrs Elborne's ability to live in the Property was clearly distinct from the Note; where Mrs Elborne lived was irrelevant to the holder of the Note. The timing of the Family Trustees' right to repayment was dependent only on her death. We do not agree with Mr Davey's submission that the application of paragraph 6 of Schedule 20 and its reference to benefits obtained by virtue of any associated operations being treated as a benefit by contract or otherwise for this purpose changes the analysis in relation to whether the relevant benefit is an integral part of the gift – as Mr Bradley put it in his submissions, paragraph 6(1) simply expands the universe in which one may search for a benefit. In consequence of this identification of the benefit and the gifted property, we agree with Mr Bradley that Mrs Elborne received no benefit referable to that which she gave.

188. It is well-established that to come within the second limb of s102(1)(b) the benefit to the donor must be something which had no existence prior to the making of the gift. This was confirmed by Henderson LJ in *Hood* where, having analysed the reasoning in the leading authorities, he stated that the central point being made in the passages to which he had referred in *Nichols* and *Ingram* was that "if the gift of a leasehold interest is accompanied by positive covenants which confer additional benefits on the donor, then there is a reservation of benefit" within s102(1)(b) ([64]) and agreed with the reasoning of Moses LJ in *Buzzoni* where Moses LJ had referred to Millett LJ's statement (dissenting in the Court of Appeal in *Ingram*) that "to come within the scope of the second limb of the subsection the benefit must consist of some advantage which the donor did not enjoy before he made the gift" and commented that this was sufficient in *Nichols* and would have been in *Ingram* ([65]).

189. On the facts here, Mrs Elborne had occupied the Property throughout, ie before the scheme was implemented, after the sale of the Property to the Life Trustees on 27 November 2003 and after the assignment of the Note to the Family Trustees (the deed for which was dated 8 December 2003 but which the FTT found did not become effective until all of the signatories executed it and that this was in late January or early February 2004 (FTT[27])).

190. Mr Davey emphasised what he submitted was the importance of the different capacity of such occupation – before November 2003 she had occupied the Property as owner of the freehold, whereas after the scheme her occupation was as holder of the interest in possession in the Life Settlement. This was, he submitted, a different interest and thus a new benefit which arose by virtue of the gift of the Note and the associated operations. We consider that this submission ignores the fact that Mrs Elborne had occupied the Property as holder of the interest in possession (ie in the same capacity as she occupied after the gift) between 27 November 2003 and late January or early February 2004 when the Note was assigned to the Family Trustees; whilst this ability to occupy did arise in this period by virtue of the associated operations, paragraph 6(1)(c) does not operate to treat the timing of the events as being different to that which actually occurred, and in this situation we conclude that the benefit to Mrs Elborne did not consist of an advantage which she did not enjoy before she made the gift of the Note.

191. We therefore agree with the FTT that the benefit was something which Mrs Elborne enjoyed before she made the gift of the Note to the Family Trustees. However, at FTT[259] the FTT had also relied on this benefit having been enjoyed before the scheme commenced. This reasoning does not have regard to the different capacities in which Mrs Elborne occupied the Property and to that extent we conclude that this reasoning involved an error of law.

192. The FTT also concluded that s102(1)(b) requires that the benefit to Mrs Elborne must have impacted upon the enjoyment by the Family Trustees of the Note in order for the Note to be treated as property subject to a reservation and that this condition was not met. We agree with the FTT's conclusion both as to the requirements of s102(1)(b) and the application to the facts.

193. Mr Davey submitted that trenching is not a necessary legislative condition, relying on Henderson LJ's reasoning at [61] in *Hood*, and submitting that this showed that whether trenching is a requirement is a case-sensitive question.

194. We do not accept Mr Davey's submissions. That there is a requirement that the benefit is one which "trenches upon" the enjoyment of the gifted property by the donee was the reasoning of Moses LJ at [50] to [57] of *Buzzoni*, and this was part of the ratio of the decision of the Court of Appeal, as this part of Moses LJ's reasoning was agreed by Black LJ and Gloster LJ. In *Hood* Henderson LJ recognised this, identifying at [52] that the outcome in *Buzzoni* had turned on the fact that the underlessees had already entered into direct covenants with the head lessor before the underlease was granted. There were no such direct covenants in *Hood*, where, instead, the benefit of the positive covenants formed an integral part of the original gift ([61]). In stating that this obviates the need "for any separate enquiry" as to whether the benefit was referable to, or trenched upon, the gift, Henderson LJ was referring to the fact that, as he framed it, "one could not have existed without the other". Henderson LJ was not saying that there is no requirement that the benefit trench upon the enjoyment of the gift; rather that the requirement is clearly satisfied where the benefit is integral to the gift.

195. Here, the benefit to Mrs Elborne did not trench upon the Family Trustees' enjoyment of the Note. As we have identified above, whilst the Note was not repayable until after Mrs Elborne's death, where Mrs Elborne lived until then had no bearing on this.

196. We therefore agree with the FTT that the second limb of s102(1)(b) does not apply to the gift of the Note. Whilst we identified above that the FTT's reasoning in FTT[259], which was then referenced in its conclusion at FTT[263(1)] involved an error of law, we have concluded that this error was not material to its decision. The FTT's separate conclusion in relation to trenching, with which we agree, is of itself sufficient to support the conclusion that the second limb cannot apply. In this situation, it cannot be said that the decision of the FTT on this issue might otherwise have been different.

*Section 102(1)(b) – exclusion of the donor (first limb)*

197. The first limb of s102(1)(b) applies if "at any time in the relevant period the property is not enjoyed to the entire exclusion, or virtually to the entire exclusion, of the donor".

198. The FTT said at FTT[256] that "there can be no dispute" about the subject-matter of the gift, namely the Note, or over whether, following the gift, the Note itself was enjoyed to the exclusion, or virtually to the entire exclusion, of Mrs Elborne. The reason it gave for this was that, following the gift, Mrs Elborne had no further interest in the Note as she was precluded from benefitting from it under the terms of the Family Settlement.

199. Mr Davey's submissions on this limb focused on the effect of the terms of the Note, coupled with Mrs Elborn's holding the interest in possession in the Life Settlement, meaning that the liability which the Note represented could not be required to be repaid prior to her death.

200. The FTT had considered the inapplicability of this first limb to be obvious, and so do we. The authorities (including *Ingram*, which concerned the application of this first limb) make clear the paramount importance of the identification of the subject-matter of the gift. The gifted property here is the Note, and that Note represents the right of the Family Trustees to be repaid

on the terms stated therein. Mrs Elborne gave the Note to the Family Trustees and was precluded from benefitting from the Family Settlement; we consider this answers the statutory question. The matters relied upon by HMRC in relation to Mrs Elborne's ability to occupy the Property can only be relevant to the application of the second limb, given that it is that limb which refers to any benefit to the donor.

201. The FTT's decision on the first limb of 102(1)(b) did not involve an error of law.

*Section 102(1)(a) – possession and enjoyment assumed by the donee*

202. Section 102(1)(a) is satisfied if "possession and enjoyment of the property is not bona fide assumed by the donee".

203. The FTT decided at FTT[261] that whilst the Family Trustees were precluded, absent a default, from demanding repayment of the Note until Mrs Elborne died, that was a function of the terms of the Note, ie the terms of the gifted property, and had no effect on the ability of the trustees to possess and enjoy the gifted property.

204. Mr Davey's submissions were based on there being no possibility of the Note being repaid until after Mrs Elborne's death, and he submitted that the FTT had erroneously imposed a trenching requirement (in FTT[261] by reference to FTT[260]). In addition, Mr Davey's oral submissions included that, following the approach in *Rossendale*, the Family Trustees could not be said to have actually possessed and enjoyed the Note in the manner intended by Parliament in a situation where the Note was a component of a scheme to avoid inheritance tax and where the Family Trustees could not do anything with that Note pending Mrs Elborne's death.

205. We do not accept Mr Davey's submissions. Once it is identified that the gifted property is the Note, there is no basis to conclude that the Family Trustees had not bona fide assumed possession and enjoyment of that gifted property. The fact that the Note was not due to be repaid until after Mrs Elborne's death was a consequence of the terms of the Note, and was not a restriction on their possession and enjoyment of the same.

206. At FTT[261] the FTT had simply said that a "similar answer" may be given to that in FTT[260], which we read as referring to the reasoning in the preceding paragraph in relation to the fact that the Family Trustees could not require repayment of the Note until Mrs Elborne had died; and this was the point which the FTT then made in FTT[261].

207. We are not persuaded that the approach of the Supreme Court in *Rossendale* assists Mr Davey in this context. The various authorities, including *Ingram*, *Buzzoni* and *Hood*, frequently involve the donor having made a gift of an asset which could have been made more valuable or attractive to the donee, the most obvious example being if the relevant sub-leases in *Buzzoni* and *Hood* had fallen into possession at an earlier date. That a different asset was gifted does not of itself mean that the donee did not assume possession and enjoyment of the property that was gifted. On the basis of the findings of fact made by the FTT, the Note gave rise to a debt on the part of the Life Trustees; once that Note was transferred by Mrs Elborne to the Family Trustees, the Family Trustees became entitled to repayment in accordance with its terms and, following Mrs Elborne's death, now have a right to receive that repayment.

208. The FTT's decision on s102(1)(a) did not involve an error of law.

209. Whilst the FTT's decision on the second limb of s102(1)(b) involved an error of law at FTT[259], such error was, as explained above, not material to the FTT's decision. The decision on the first limb of s102(1)(b) and on s102(1)(a) did not involve an error of law. HMRC's cross-appeal on the Section 102 Note Issue is dismissed.

**DISPOSITION**

210. Section 12(2) Tribunals, Courts and Enforcement Act 2007 provides that if the Upper Tribunal finds that the making of the decision under appeal involved the making of an error on a point of law then the Upper Tribunal "may (but need not)" set aside the decision of the FTT.

211. We have concluded that the decision of the FTT on the Section 103 Debt Incurred Issue involved two errors of law. Individually and together, those errors were material to the FTT's conclusion on that issue and to the appeal. We set aside the Decision.

212. We re-make the decision on the basis of the facts as found by the FTT.

213. For the reasons set out above, we have allowed the Appellants' appeal on the Section 103 Debt Incurred Issue. This was the only ground on which the Appellants were unsuccessful before the FTT. We have dismissed HMRC's cross-appeal on all five grounds.

214. For the reasons set out in our discussion of each of the six issues which were live in this appeal, the Appellants' appeal against the notices of determination is allowed.

**JUDGE JEANETTE ZAMAN**
**JUDGE VIMAL TILAKAPALA**

**UPPER TRIBUNAL JUDGES**

**Release date: 17 February 2025**