

INHERITANCE TAX: OMISSIONS ARE NOT ACCIDENTS?

RACHEL Staveley died on 18 December 2006. HMRC raised notices of determination to Inheritance Tax (IHT) on her executors (“the taxpayers”) on the basis that she had made two (non-overlapping) lifetime transfers of value on which tax was chargeable. First, a transfer of value when she transferred her pension fund from an existing (post-divorce) policy associated with the company she had run with her ex-husband to a new personal pension scheme (“the Transfer”). The post-divorce pension scheme provided for death benefits to be paid to her personal representatives and benefit her sons via her estate but there was also a perceived risk that a surplus would benefit her ex-husband (towards whom Mrs. Staveley felt bitter). The second transfer of value was immediately prior to her death, which was the last point at which she could have drawn lifetime benefits under that new private pension but she omitted to do so (“the Omission”). Those death benefits were held subject to a discretion in the hands of the new private pension trustees, who implemented her non-binding nomination in favour of her sons.

It was clear that the Transfer caused a loss to Mrs. Staveley’s estate within the meaning of section 3(1) IHTA 1984. In those circumstances, there were three important points with which the Supreme Court had to grapple:

- (1) Was the Transfer, viewed on its own, within section 10(1) IHTA 1984, because it was not intended to confer any gratuitous benefit, thus escaping IHT?
- (2) If so, was the Omission an associated operation (defined by s. 268 IHTA 1984 and applied by s. 10(3) IHTA 1984) so that when the Transfer viewed in its wider context showed an intention to confer a gratuitous benefit, thereby causing a charge to IHT?
- (3) Was an increase in another person’s estate caused by the Omission and therefore a transfer of value under section 3(3) IHTA 1984 (and as such subject to tax)?

The Supreme Court in *Revenue and Customs Commissioners v Parry* [2020] 1 W.L.R. 3692 (Lord Reed, Lady Black and Lord Kitchin with Lords Hodge and Sales dissenting regarding associated operations) held that the Transfer either viewed on its own or in a wider context of the Omission was not intended to confer a gratuitous benefit. However, the Omission was a transfer of value for the purposes of section 3(3). The result was essentially a score draw between the taxpayers and the Revenue, nevertheless it did leave the taxpayers in a better position than before the Court of Appeal.

It is worth noting that, following the introduction of section 12(2ZA) IHTA 1984 by the Finance Act 2011, an omission to exercise pension rights in registered pension schemes no longer triggers an IHT liability. Equally, the intention of Mrs. Staveley and her particular motivation to avoid benefiting her ex-husband, is an unusual fact pattern. Nevertheless, *HMRC v Parry* leaves an important, if not especially clear, legacy in its analysis of intention to confer a gratuitous benefit within the meaning of section 10(1); the analysis of associated operations within the meaning of section 10(3) and the analysis of the House of Lords' decision in *IRC v Macpherson* [1989] A.C. 159.

On the issue of intention to confer a gratuitous benefit under section 10 (1) the taxpayers argued, based on facts found at first instance, that Mrs. Staveley had not intended to benefit her sons by the Transfer. She wished to avoid any benefit to her ex-husband and the First Tier Tribunal found this was her sole motive in making the Transfer. The executors' argument was based on the substance and the fact that Mrs. Staveley did not believe she was changing her sons' position. HMRC's approach involved what was described by Lady Black as "return to zero" (at [57]) reliant on a moment in time before the rights under the old pension ended and the new rights began. HMRC's argument was in difficulty because of the finding that Mrs. Staveley's sole motive was to sever links with the company.

The Supreme Court adopted the reasoning of Newey L.J. in the Court of Appeal; that it was appropriate to look to the intention "by the overall effect of the disposition" to benefit the recipient gratuitously. With regard to the conferring of a benefit the court had to consider whether there was any intention to improve the beneficiary's position via the transaction as compared with the original position. The legal analysis of rights was relevant but it was important to consider the practical reality of the situation. The Supreme Court's conclusion is unsurprising as HMRC's technical approach had an element of *Ramsay* in reverse (*WT Ramsay v IRC* [1982] A.C. 300). It is usually HMRC that prosecutes appeals based on substance not form. Furthermore, had HMRC's argument succeeded, it might have prevented section 10(1) applying to an unintentional sale at an undervalue, which is a core case where one would expect section 10(1) to apply: see [60].

The most interesting and important aspect of the case was the majority and dissenting views on the concept of associated operations under section 10(3) IHTA 1984. The parties disagreed as to the proper interpretation of *Macpherson*. That case concerned capital transfer tax. It involved materially similar provisions to the IHTA 1984, the variation of an agreement in relation to the custody and insurance of paintings held by a settlement, which substantially diminished their value. and the day after the variation, the exercise of a power of appointment over the paintings. The appointment would not have been made in the absence of the variation. There was a clear

link between the steps by a common intention (at [83]) and a scheme of associated operation was formed.

In *Macpherson* Lord Jauncey of Tullichettle explained ([1989] A.C. 159, at 175) that

If the extended meaning of “transaction” is read into the opening words of section 20(4) [Finance Act 1975] the wording becomes:

“A disposition is not a transfer of value if it is shown that it was not intended, and was not made in a transaction including a series of transactions and any associated operations intended, to confer any gratuitous benefit . . .”

So read it is clear that the intention to confer gratuitous benefit qualifies both transactions and associated operations. If an associated operation is not intended to confer such a benefit it is not relevant for the purpose of the subsection. That is not to say that it must necessarily per se confer a benefit but it must form a part of and contribute to a scheme which does confer such a benefit.

The taxpayers argued that *Macpherson* required a “scheme” comprising the Transfer and the Omission *and* that each element of the scheme was required to have an intention of gratuitous benefit. HMRC recognised the need for a scheme, but submitted that in this case the scheme was to benefit Mrs. Staveley’s sons by way of death benefits to which both the Transfer and also the Omission contributed. HMRC argued that there was a link between the steps by reason of a common intent.

The majority agreed with HMRC that it was not necessary for each element of the scheme to be made with an intention gratuitously to benefit a person; nevertheless the majority did not consider that there was a sufficient connection between the Transfer and the Omission for them to be associated operations as a contributory part of a scheme intended to confer a gratuitous benefit (at [77]). Mrs. Staveley had already decided not to exercise her rights to call for pension benefits, namely not to take lifetime benefits, so as to advantage her sons when she executed the Transfer. The Transfer was not necessary to achieve that. The Transfer was necessary to avoid benefit to the ex-husband. Therefore the Transfer and the Omission were not relevantly associated. It is not entirely clear what Lady Black meant by “relevantly associated” (at [88]).

Her view can be contrasted with that of Lord Hodge, dissenting with Lord Sales. He considered that the majority’s view inserted a test of “necessity” (i.e. that each step of the scheme was necessary to obtain the desired gratuitous benefit) into Lord Jauncey’s analysis which it did not truly contain (at [108]). Lord Hodge considered that the Transfer was “referable to and formed a contributory part” of a substituted scheme to enable the sons to obtain the death benefits (at [109]).

The Supreme Court held unanimously that the Omission constituted a transfer of value for the purposes of section 3(3). The taxpayers argued

that section 3(3) requires an immediate and direct, causally linked, increase in another person's estate (rather than a "but for" increase) as a result of an omission. They argued that the fact that the private pension trustees had a discretion whether or not to follow Mrs. Staveley's non-binding nomination broke the chain of causation. Lady Black held that this argument failed as it was too technical and legalistic.

Of the three issues that faced the court, it is the second concerning associated operations which is likely to have the greatest influence on IHT. Whereas the case has provided some important exploration of the concept of association, Lady Black's formulation of "relevantly associated" is plainly question begging.

RUTH HUGHES

Address for Correspondence: 5 Stone Buildings, Lincoln's Inn, London, WC2A 3XT, UK. Email: rhughes@5sblaw.com

CONTRACTUAL VARIATIONS: LONG LIVE THE DOCTRINE OF CONSIDERATION?

IN the realm of contract law, the doctrine of consideration has fascinated many for centuries and has unsurprisingly generated a wealth of commentary. While the doctrine has withstood the test of time in so far as the formation of contracts is concerned, serious doubts have been cast over its continued "reign" in the context of contractual variations. In 2018, the UK Supreme Court in *Rock Advertising Ltd. v MWB Business Exchange Centres Ltd.* [2018] UKSC 24 decided that it was "unnecessary" and "undesirable" to deal with the "difficult" issue of whether the oral variation was supported by consideration given that the variation was invalid for want of the writing and signatures required under the licence agreement (at [17]–[18]). Many were understandably disappointed by the UK Supreme Court's failure to deal directly with the issue of consideration (Janet O'Sullivan, "Party-Agreed Formalities for Contractual Variation: A Rock of Sense in the Supreme Court?" (2019) 135 L.Q.R. 1, 6). Very recently, a specially constituted five-judge bench of the Singapore Court of Appeal in *Ma Hongjin v SCP Holdings Pte Ltd.* [2020] SGCA 106 had occasion to consider whether the time has come for the doctrine of consideration to be abolished with regard to contractual variations. This decision is particularly significant because of the reasons given by the Singapore apex court in favour of retaining the doctrine even in the context of contractual variations.

Ma Hongjin involved a convertible loan agreement which was entered into between the appellant and the respondent on 6 January 2015. Under the convertible loan agreement, the respondent had to pay interest at the rate of 10 per cent per annum in exchange for the appellant's extension of a S\$5 million loan for a period of two years. Subsequently, the parties