TC00667

Appeal number: TC/2009/10161

Income tax – gift aid – s 25 FA 1990 – gifts to charity under deed of variation of a deceased's estate – s 142 IHTA 1984 – - whether gift a qualifying donation - whether donors received a benefit in consequence of making the gifts – s 25(2)(e) FA 1990

FIRST-TIER TRIBUNAL

TAX

RONALD MICHAEL HARRIS
(as trustee of the Harris Family Charitable Trust) **Appellant**

- and -

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

TRIBUNAL: JUDGE ROGER BERNER
DAVID E WILLIAMS CTA (Member)

Sitting in public at 45 Bedford Square, London WC1 on 27–28 July 2010

Giles Goodfellow QC and Thomas Chacko, instructed by Harris & Trotter LLP, for the Appellant

Matthew Smith, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. This is an appeal by Mr Ronald Harris as trustee of the Harris Family Charitable Trust ("the Charity") against income tax assessments for the years of assessment 2004/05 and 2005/06. The purpose of the assessments is to recover repayments of basic rate income tax made to the Charity in respect of gifts of cash made to the Charity during those years of assessment.

2. Mr Harris and his sister, Mrs Fine, each obtained higher rate income tax relief in respect of the grossed up value of the gifts made to the Charity. Although no assessments have been made upon Mr Harris or Mrs Fine in this respect, we understand that it has been agreed by the parties that their liability to repay such relief will be determined in accordance with the outcome of this appeal.

3. The gifts in question were not made by Mr Harris and Mrs Fine directly to the Charity. Those gifts arose out of a deed of variation of the will of their late mother, Mrs Ruth Harris. The question we have to consider in this appeal is whether the inheritance tax exemption that became available by virtue of that deed of variation has the effect, for the reasons we shall explain, of preventing the gifts to the Charity from being "qualifying donations" within section 25 of the Finance Act 1990 ("FA 1990"), and so not being eligible for the tax reliefs afforded by that section.

4. Giles Goodfellow QC and Thomas Chacko appeared for the Appellant. The Respondents were represented by Matthew Smith.

The facts

5. There was no dispute on the facts. We had a short statement of facts not in dispute, which we reproduce below. In addition we had an unchallenged witness statement of Mr Harris, and an agreed bundle of documents.

Statement of facts not in dispute

1. The late Mrs Elizabeth Ruth Harris ("Testatrix") died on 29 January 2004. By her Will dated 8 December 1998 and in the events which occurred the residue of her estate was left to her two surviving children, Ronald Michael Harris ("Mr Harris") and Irene Valerie Fine ("Mrs Fine") in equal shares absolutely. Due to her husband Alfred Harris's earlier death on 9 January 2000, the prior life interest in his favour did not take effect.

2. Probate was granted on 9 August 2004 to Mr Harris, Mrs Fine and Malcolm Webber as Executors and Trustees of the Will. The net estate was valued at £4,170,180.

3. By a Deed of Variation dated 25 February 2004 executed between (1) Mr Harris and Mrs Fine as beneficiaries of the Will and (2) Mr Harris, Mrs Fine and Mr Webber as executors and trustees of the Will, it was recorded that:

- Mr Harris and Mrs Fine were each given an absolute half interest in the Testatrix's residuary estate;

- Each of them wished to vary the dispositions of property effected by the Will in relation to their interests in residue.
- Mr Harris and Mrs Fine directed that the provisions of the Will should take effect as if it had provided for the payment of a legacy of £500,000 to the Harris Family Charitable Trust ("the Charitable Trust") out of Mr Harris's share of the residue of the estate and for the payment of a legacy of £50,000 to the Charitable Trust out of Mrs Fine's half share in the residuary estate.
- The parties to the Deed intended that the provisions of s142(1) of the Inheritance Tax Act 1984 and of section 62(6) of Taxation of Chargeable Gains Act 1992 should apply to the deed of variation.

4. The Charitable Trust was established on 1 April 1997 by way of a Deed of Variation executed between (1) the Testatrix as beneficiary and (2) the Testatrix and Mr Harris as the initial Trustees . The present Trustees are Mr Harris, his wife Mrs L M V Harris and his daughter Ms C Harris.

5. In the Executors' IHT Account filed with HMRC in July 2004 the legacies payable to the Charitable Trust pursuant to the deed of variation were treated as passing by way of exempt transfers of value. The claim for exemption was accepted by HMRC and on or about 25 June 2006 a certificate of discharge was issued by HMRC to the Executors.

6. Pursuant to directions made by Mr Harris and Mrs Fine and as and when the Executors were able to realise assets to make cash distributions, the Executors made the following payments to the Charitable Trust:

21 December 2004	£250,000 (all re Mr Harris)
20 July 2005	£150,000 (all re Mr Harris)
26 January 2006	£150,000 (both Mr Harris and Mrs Fine)

These payments were all treated by both the Charitable Trust and Mr Harris and Mrs Fine as being made under gift aid. The relevant tax refund claims were submitted by the Charity on forms R68. A refund of £70,597.44 was received from HMRC on 13 June 2005 in respect of the claim for 2004/05 and a refund of £84,615.38 was received from HMRC on 15 March 2007 by the Charitable Trust in respect of the claim for 2005/06. On the basis that the payments to the Charitable Trust were treated as "qualifying donations" for Gift Aid purposes, Mr Harris received income tax relief in the approximate sum of £115,384 in respect of the tax years 2003/04 and 2004/05, and Mrs Fine received income tax relief in the approximate sum of £11,538 in respect of the tax year 2004/05.

7. By their letter of 12 June 2007 H M Revenue & Customs launched an enquiry into the 2005/06 repayment claim by the Charity. On 9 April 2009 HMRC issued assessments for 2004/05 and 2005/06 on the Charitable Trust to recover the repayments of basic rate income tax previously made to the Charitable Trust. An Appeal was lodged by the Charitable Trust with the Tribunal on 1 May 2009.

6. The witness statement of Mr Harris provided further background information. In particular it confirmed, which was not in dispute, the status of the Charity as an exclusively charitable trust and the intention of Mr Harris and Mrs Fine to make gifts of money to the Charity out of their respective shares of the residue of their late mother's estate.

The law

7. Relief for cash gifts to charity by individuals is given by s 25 FA 1990, the material parts of which are:

> "**25 Donations to charity by individuals**
>
> (1) For the purposes of this section, a gift to a charity by an individual ("the donor") is a qualifying donation if—
>
> (*a*) it is made on or after 1st October 1990,
>
> (*b*) it satisfies the requirements of subsection (2) below, and
>
> (*c*) the donor gives an appropriate declaration in relation to it to the charity.
>
> (2) A gift satisfies the requirements of this subsection if—
>
> (*a*) it takes the form of a payment of a sum of money;
>
> …
>
> (*e*) neither the donor nor any person connected with him receives a benefit in consequence of making it or, where the donor or a person connected with him does receive a benefit in consequence of making it, the relevant value in relation to the gift does not exceed the limit imposed by subsection (5A) below and the amount to be taken into account for the purposes of this paragraph in relation to the gift does not exceed £250;
>
> …
>
> (*i*) either—
>
> (i) at the time the gift is made, the donor is resident in the United Kingdom or is in Crown employment as defined in section 28(2) of the Income Tax (Earnings and Pensions) Act 2003; or
>
> (ii) the grossed up amount of the gift would, if in fact made, be payable out of profits or gains brought into charge to income tax or capital gains tax.
>
> …
>
> (5A) The limit imposed by this subsection is—

(*a*) where the amount of the gift does not exceed £100, 25 per cent of the amount of the gift;

(*b*) where the amount of the gift exceeds £100 but does not exceed £1,000, £25;

(*c*) where the amount of the gift exceeds £1,000, 2.5 per cent of the amount of the gift.

…

(5E) In determining whether a gift to a charity falling within subsection (5F) below is a qualifying donation, there shall be disregarded the benefit of any right of admission received in consequence of the making of the gift—

(*a*) to view property the preservation of which is the sole or main purpose of the charity; or

(*b*) to observe wildlife the conservation of which is the sole or main purpose of the charity;

but this subsection shall not apply unless the opportunity to make gifts which attract such a right is available to members of the public.

(5F) A charity falls within this subsection if its sole or main purpose is the preservation of property, or the conservation of wildlife, for the public benefit.

(5G) In subsection (5E) above "right of admission" refers to admission of the person making the gift (or any member of his family who may be admitted because of the gift) either free of the charges normally payable for admission by members of the public, or on payment of a reduced charge.

(6) Where any gift made by the donor in a year of assessment is a qualifying donation, then, for that year—

(*a*) the Income Tax Acts and the Taxation of Chargeable Gains Act 1992 shall have effect, in their application to him, as if—

(i) the gift had been made after deduction of income tax at the basic rate; and

(ii) the basic rate limit were increased by an amount equal to the grossed up amount of the gift;

(*b*) the provisions mentioned in subsection (7) below shall have effect, in their application to him, as if any reference to income tax which he is entitled to charge against any person included a reference to the tax treated as deducted from the gift; and

(*c*) to the extent, if any, necessary to ensure that he is charged to an amount of income tax and capital gains tax equal to the tax treated as deducted from the gift, he shall not be entitled to relief under Chapter I of Part VII of the Taxes Act 1988;

but paragraph (*a*)(ii) above shall not apply for the purposes of any computation under sections 535 to 537 of the Income Tax (Trading and Other Income) Act 2005 (top slicing relief).

(7) The provisions referred to in subsection (6)(*b*) above are—

(*a*) section 289A(5)(*e*) of the Taxes Act 1988 (relief under enterprise investment scheme);

(*b*) section 796(3) of that Act (credit for foreign tax);

(*c*) paragraph 1(6)(*f*) of Schedule 15B to that Act (venture capital trusts) and

(*d*) paragraph 19(6)(*d*) of Schedule 16 to the Finance Act 2002.

(8) Where the tax treated as deducted from a gift by virtue of subsection (6) above exceeds the amount of income tax and capital gains tax with which the donor is charged for the year of assessment, the donor shall be assessable and chargeable with income tax at the basic rate on so much of the gift as is necessary to recover an amount of tax equal to the excess.

…

(11) Section 839 of the Taxes Act 1988 applies for the purposes of subsections (2) and (4) above.

(12) For the purposes of this section—

…

(*c*) "relevant year of assessment", in relation to a gift, means the year of assessment in which the gift is made;

…"

8. This version of s 25 is that applicable for tax year 2005/06. For 2004/05, there was only one difference, which is not material: in s 25(6) for the references to provisions in ITTOIA (the Income Tax (Trading and Other Income) Act 2005), the wording is to the superseded provisions of the Taxes Act 1988, "section 550(2)(a) or (b) of that Act (relief where gain charged at a higher rate)".

9. Section 25 provides for income tax (and, at the relevant time, CGT) relief for a gift to charity that qualified as a "qualifying donation". There is no dispute on any of the requirements of s 25(2), except in relation to s 25(2)(e). The dispute is whether the donors, or a person connected with the donors, received a benefit in consequence of making the gifts to the Charity. If such a benefit was received, it is common ground that it would exceed the de minimis limits, and would thus prevent the gifts being qualifying donations.

10. The deed of variation was effected under s 142 of the Inheritance Tax Act 1984 ("IHTA"), the material parts of which are:

"**142 Alteration of dispositions taking effect on death**

(1) Where within the period of two years after a person's death—

(*a*) any of the dispositions (whether effected by will, under the law relating to intestacy or otherwise) of the property comprised in his estate immediately before his death are varied, or

(*b*) the benefit conferred by any of those dispositions is disclaimed,

by an instrument in writing made by the persons or any of the persons who benefit or would benefit under the dispositions, this Act shall apply as if the variation had been effected by the deceased or, as the case may be, the disclaimed benefit had never been conferred.

(2) Subsection (1) above shall not apply to a variation unless the instrument contains a statement, made by all the relevant persons, to the effect that they intend the subsection to apply to the variation.

(2A) For the purposes of subsection (2) above the relevant persons are—

(*a*) the person or persons making the instrument, and

(*b*) where the variation results in additional tax being payable, the personal representatives.

Personal representatives may decline to make a statement under subsection (2) above only if no, or no sufficient, assets are held by them in that capacity for discharging the additional tax.

…

(6) Subsection (1) above applies whether or not the administration of the estate is complete or the property concerned has been distributed in accordance with the original dispositions.

…"

11. It can be seen, and this was again common ground, that for inheritance tax purposes the variations of the dispositions of a deceased's estate by means of a deed of variation are treated as having been effected by the deceased and not by the beneficiaries of the dispositions. Furthermore, it is only necessary under s 142 for the statement confirming the intention that s 142(1) should apply to be made by the personal representatives if the variation will result in additional tax being payable. Finally, the deed has its deeming effect whether or not the administration of the estate is complete or if the property has been distributed in accordance with the original dispositions.

12. On the death of a person there is a deemed transfer of value immediately before death, and the value transferred is treated as equal to the then value of the estate (s 4(1) IHTA. As a result of the deed of variation, that transfer of value was treated as having included the legacies to the Charity. By s 23 IHTA, the transfer of value on death is exempt to the extent that the value transferred is attributable to property given to charities. In the case of a legacy to a charity, which is a specific gift, the value transferred is equal to the value of the gift, and that is the extent of the exemption (s 38). Section 41 IHTA then provides that, notwithstanding the terms of any disposition, none of the tax on the value transferred is to fall on any specific gift if or to the extent that the transfer is exempt with respect to that gift. The effect is that the tax on the value transferred on the death of the testatrix following the deed of variation fell solely on the residuary estate, and not on the gifts to the Charity. For IHT purposes therefore the effect of the variation was that no charge to IHT ever fell on the gifts to the Charity.

13. That deals with where the burden of IHT falls. There is then the question of liability for the tax. Section 200 IHTA makes provision for liability in the cases of transfer on death. Except in most cases of settled property, liability falls on the personal representatives and, in broad terms, the beneficiaries in whom property is vested, so far as the tax is attributable to the value of that property. Thus, in the case of the estate of the testatrix, liability for the tax on the residuary estate following the variation fell on the executors and on Mr Harris and Mrs Fine as residuary beneficiaries. The deeming effect of the deed of variation meant that, although Mr Harris and Mrs Fine became respectively entitled to the amounts directed by them to pass to the Charity as specific gifts, because for IHT purposes the tax on the amount of the value transferred attributable to those exempt gifts is treated as not having arisen, then for the purposes of IHT they did not as residuary beneficiaries ever become liable for that tax.

14. So far as the liability of the personal representatives is concerned, this is subject to the limitation in s 204(1) IHTA. Disregarding settled property, recourse can only be had to the assets which the personal representatives have received in that capacity, or might have so received but for their own neglect or default. Subject to the deceased's will, the tax is treated as part of the general testamentary and administration expenses of the estate so far as it is attributable to the value of property in the UK which vests in the personal representatives (s 211), and a personal representative has the power to raise the tax attributable to the value of any property out of that property (s 212(1)). In similar vein, the liability of a beneficiary is limited to the extent of the property vested in that beneficiary (s 204(3)).

Discussion

15. This is a case of statutory construction. In its narrowest sense what is required to be construed is s 25(2)(e) FA 1990. Taxing statutes have to be construed purposively according to the reality of the arrangements in question (see *Barclays Mercantile Business Finance Ltd v Mawson (Inspector of Taxes)* [2005] STC 1 at [32]). The ultimate question is whether the relevant statutory provisions, construed purposively, are intended to apply to the transaction viewed realistically (*Collector of Stamp Revenue v Arrowtown Assets Ltd* [2003] HKCFA 46; 6 ITLR 454 at [35] per Ribeiro PJ).

Non-statutory material

16. Mr Goodfellow submitted that the relevant statutory provisions required to be considered in context. He referred us to press releases issued by the (as it then was) Inland Revenue at the time of the Budget on 20 March 1990 and the tabling on 15 June 1990 of new clauses to the Finance Bill of that year in respect of the gift aid proposals. He also drew our attention to the Hansard report of the debates in the Standing Committee E on 28 June 1990 in respect of what became s 25 FA 1990.

17. It was common ground that the press releases were admissible in evidence. In the first of these, on Budget day, 20 March 1990, it was stated that the Chancellor had proposed a range of measures to encourage individual and corporate charitable giving. Included amongst the new measures was gift aid, described as an entirely new income tax relief for single gifts by individuals which equalled or exceeded the new £600

ceiling for payroll giving. In the details given of this new relief, reference was made to certain restrictions that would apply:

> "There will be rules to ensure that gifts will not qualify for the relief if they are linked with any purchase of property from the donor, or if they are not outright gifts (for example, they are payments to charities in return for services or benefits)."

18. A second press release was issued on 15 June 1990 to announce the tabling by the Government of the new clauses to the Finance Bill introducing gift aid. This explained that to qualify for the new relief a gift must be a gift of money, but that it must not be either:

> "- linked with the acquisition of property by the charity, otherwise than by way of gift from the donor or a person connected with him; or
>
> - made for the supply of services or other benefits for the donor or any person connected with him."

19. We have derived no assistance from these press releases in construing the statutory provisions before us. As to mischief, in our view the only mischief identified by the press releases is the former restriction on relief for individual gifts to charity which the new gift aid was intended to address, subject to a number of limitations. We do not regard the very brief descriptions of the proposed restrictions as in any way exhaustive or definitive or as intended to be specific as to the interpretation of the statutory provisions. In our view, any reliance on the descriptions given in the press releases would effectively amount to substituting the Inland Revenue's brief description for the statutory words themselves. We consider that the proper approach is to construe the statute and not extraneous material such as the press releases.

20. Different considerations apply to the Parliamentary debates in Standing Committee E as reported in Hansard. In *Pepper v Hart* [1993] AC 593, the House of Lords (by a majority) held that, subject to any question of Parliamentary privilege, the former rule excluding reference to Parliamentary material as an aid to statutory construction should be relaxed so as to permit such reference where (a) legislation was ambiguous or obscure or led to absurdity, (b) the material relied upon consisted of one or more statements by a Minister or other promoter of the Bill together, if necessary, with other Parliamentary material as was necessary to understand such statements and their effect and (c) the statements relied upon were clear.

21. The statements to which Mr Goodfellow referred us were made by the then Economic Secretary to the Treasury (Mr Richard Ryder). In responding to an Opposition tabled amendment to the original drafting of what became s 25(2)(e) to limit the disqualifying benefits to material benefits of more than 5% of the grossed up amount of the gift, and to tax the value of a non-material benefit, the Economic Secretary said:

> "[The relevant proposed amendments] are concerned with cases where the donor receives some benefit in return for his donation. I understand the thinking behind the amendments, but they would

> introduce a new element of undue complexity, which would detract from this very simple scheme. One of its great merits is that those who wish to give to charity can do so, because they understand the scheme. My right hon. Friend the Chancellor is determined that the scheme should be kept as simple as possible, so I cannot accept the amendment.
>
> New clause 40, under which donors must get no benefit in return for their gifts, is clear and unambiguous. If donors want to make separate arrangements with charities to pay for goods and services supplied by a charity, they are free to do so, but they should keep such arrangements apart from their gift and gifts. If they do not, complications may be introduced into an otherwise straightforward scheme."

22. As with the press releases, we derive no assistance from this Parliamentary material in construing s 25. We do not regard the Economic Secretary's reference to payments for goods and services supplied by a charity as in any way limiting, or as intended as a limitation on, the meaning of s 25(2)(e). Nor do we consider that the references to the scheme being a simple and straightforward one can affect the way it is to be construed. However simple and straightforward a statutory provision might be intended to be, in the real world the way in which it is sought to be applied by taxpayers may be anything but simple. Indeed, the Economic Secretary himself recognised that complexity might be introduced depending on the way taxpayers behaved.

23. In any event, for the reasons we shall explain later, we do not regard s 25 as giving rise to any ambiguity, obscurity or absurdity such as to satisfy the *Pepper v Hart* test and permit us to consider the Parliamentary material.

The issues

24. It was common ground before us, and we agree, that, as a matter of general law, the deed of variation took effect as directions to the executors to make gifts of cash at a future time or times on behalf of Mr Harris and Mrs Fine out of their respective entitlements as residuary beneficiaries. Accordingly, each of Mr Harris and Mrs Fine, as individuals, were the donors for the purpose of s 25(1) FA 1990. There was no argument, rightly in our view, that the executors should be regarded as the donors.

25. As such, the issue is whether each of the donors, or a person connected with a donor, has received a benefit prohibited by s 25(2)(e) because either:

(1) the IHT for which they would have been liable as personal representatives has been reduced in consequence of the cash gifts made pursuant to the deed of variation; or

(2) the donors, as residuary beneficiaries of the estate, have been able to make or procure the making of a cumulative contribution to the Charity of £550,000 without bearing IHT in an amount equal to the value of the reduction in the IHT liability.

Benefit as personal representatives

26. Mr Smith argued that since the liability to IHT was a personal liability of the personal representatives, the removal of that liability by virtue of the deed of variation under s 142 IHTA was a benefit received by the personal representatives. He relied upon *IRC v Stannard* [1984] STC 245 which held, as regards the equivalent legislation concerning capital transfer tax, that a charge to that tax arising on death could not have been a liability of the deceased. It was an original liability of the deceased's personal representatives. Although s 27(1) FA 1975 (the precursor to s 204(1) IHTA) provided for a limitation of liability to which personal representatives might otherwise be exposed, this did not limit the liability of a personal representative to liability in a personal representative capacity only. The liability of a personal representative is accordingly a personal liability.

27. Mr Goodfellow argued that *Stannard* was concerned with the question of the nature of a personal representative's liability, and not that of the burden of IHT or the benefit of the removal of such a liability. He referred us to *Daniels v Thompson* [2004] EWCA Civ 307 in support of his proposition that, as the liability of the personal representatives of a deceased is limited by s 204(1) IHTA to the assets of the estate falling into the hands of the personal representatives, and that by s 211, absent any contrary intention of the testator, the tax is treated as part of the general testamentary and administration expenses of the estate so far as attributable to UK property (other than settled property) that vests in the personal representatives, an IHT liability could not result in a loss to the personal representatives, and consequently a reduction in IHT liability could not give rise to a benefit.

28. We prefer Mr Goodfellow's argument on this to that of Mr Smith. In our view the structure of the IHT legislation in respect of the liability of personal representatives, in particular sections 204(1) and 211 IHTA, makes it inapt to describe a reduction in an IHT liability of the personal representatives as a benefit to them in that capacity. In the same way that, in *Daniels v Thompson*, an increased liability to IHT did not result in the personal representative, notwithstanding that the liability was personal to him, suffering a loss in his capacity as such, so too a reduction in IHT is not a benefit received by the personal representatives in that capacity.

29. That would dispose of the question of benefit in the case of the executors, but, because we heard argument on the point, we ought also to consider whether, had we decided that the executors received a benefit as such, that benefit would thereby have been received, as required by s 25(2)(e) FA 1990, by a person connected with Mr Harris and Mrs Fine as the donors.

30. The definition of connected persons for this purpose is to be found in s 839 of the Income and Corporation Taxes Act 1988 ("Taxes Act") (see s 25(11) FA 1990). That section, so far as material, provides:

> "**839 Connected persons**
>
> (1) For the purposes of, and subject to, the provisions of the Tax Acts which apply this section, any question whether a person is connected with another shall be determined in accordance with the following

provisions of this section (any provision that one person is connected with another being taken to mean that they are connected with one another).

(2) A person is connected with an individual if that person is the individual's spouse or civil partner , or is a relative, or the spouse or civil partner of a relative, of the individual or of the individual's spouse or civil partner .

(3) A person, in his capacity as trustee of a settlement, is connected with—

(*a*) any individual who in relation to the settlement is a settlor,

(*b*) any person who is connected with such an individual, and

(*c*) any body corporate which is connected with that settlement.

In this subsection "settlement" and "settlor" have the same meaning as in Chapter 5 of Part 5 of ITTOIA 2005 (see section 620 of that Act)."

In s 839(3), the reference to ITTOIA was inserted with effect, for income tax purposes, for the tax year 2005/06 and subsequent years. Formerly, and accordingly for 2004/05, the reference was to Chapter 1A of Part XV of the Taxes Act (see s 660G(1) and (2)). There is no material difference in this for the purpose of our decision.

31. Mr Smith argued that, since Mr Harris and Mrs Fine were themselves the personal representatives of their late mother's estate (along with Mr Webber), and they had a personal liability as such, and on the assumption they had received a benefit in that capacity, s 25(2)(e) was satisfied directly, and without recourse to the connected persons rules. We do not accept this. There must be a distinction between a benefit being received by an individual beneficiary and a benefit being received, albeit by the same person, in a representative capacity, notwithstanding that, on the basis of *Stannard*, the underlying liability to IHT is a personal liability of the personal representatives. Otherwise a different result would obtain depending on whether the residuary beneficiaries were the same persons as, or different persons from, the personal representatives.

32. Mr Smith submitted further that, if s 839 applied, the relevant rule was that contained in s 839(2) and not, as Mr Goodfellow argued, s 839(3). We are satisfied that in these circumstances it is s 839(3) that is applicable, and not s 839(2). It is clear that s 839 draws a distinction between a person in an individual capacity, and the same person in a representative, or fiduciary, capacity. The reference to a person in s 839(2) is to that person in the capacity that would enable him or her to be the husband or wife of an individual or otherwise related in the terms of s 839(2). Section 839(3) relates to persons in a different capacity, thus making it clear that it is the capacity in which a person acts that creates the distinction. The capacity in s 839(3) is a wide one, depending as it does on the income tax definition of "settlement" which, in s 620 ITTOIA includes "any disposition, trust, covenant, agreement, or transfer of assets …" This definition is apt to include the disposition by will of a deceased's estate, and the personal representatives are the trustees of that "settlement". Accordingly it is s 839(3) that must be applied if any connection is to be established between the

personal representatives (which include Mr Harris and Mrs Fine) and Mr Harris and Mrs Fine as individuals.

33. The "settlor" for this purpose was the testatrix, Mrs Ruth Harris. The only question is whether s 839(3)(b) can apply, so that Mr Harris and Mrs Fine, as the lineal descendants of Mrs Ruth Harris, are at the relevant time to be treated as connected to their late mother. In our view there can be no such connection with a deceased person. Section 839(3)(b) is expressed in the present tense, and s 839(3)(a) requires the settler at the relevant time to be an individual who *is* the settlor. None of this is apt to include a deceased settlor. Accordingly, were we to have found that the personal representatives received a benefit, we would have concluded that those personal representatives were not connected with either of Mr Harris or Mrs Fine as donors, so that the receipt of such a benefit would not have fallen within s 25(2)(e) FA 1990.

Benefit as residuary beneficiaries

34. We turn therefore to what we consider to be the real dispute between the parties: whether Mr Harris and Mrs Fine, as the donors of the charitable gifts, received a benefit in consequence of making those charitable gifts.

35. This question has been considered before, by a Special Commissioner (Mr David Shirley) in *St Dunstan's v Major (Inspector of Taxes)* [1997] STC (SCD) 212. In that case a sole residuary legatee of his late mother's will executed a deed of variation by which he declared that the will should have effect as if it had included a legacy of £20,000 to St Dunstan's, a registered charity. An election was made under s 142 IHTA, and a saving of £8,000 of IHT was achieved. The Inland Revenue concluded that this sum was not a qualifying donation within s 25 FA 1990, essentially on the ground that the donor had received a benefit in consequence of the making of the gift. It was held by the Special Commissioner that s 25(2)(e) was not confined to benefits provided by the charity itself. As the donor was the sole residuary beneficiary of the estate, he had ultimately benefitted from the IHT saving. That benefit had arisen in consequence of making the gift by means of the deed of variation.

36. Although we should pay due regard to decisions of the special commissioners, we are not bound by them. In this case we have heard full argument on the construction of s 25 by reference to first principles. Accordingly, although the facts in *St Dunstan's* are markedly similar to those of this case, we make our own determination in this appeal, by reference to our own construction of s 25, and the application of that provision, so construed, to the facts of this case.

37. Each of Mr Goodfellow and Mr Smith argued their respective cases on the footing that there were a number of separate elements to be considered in determining whether or not s 25(3)(e) was satisfied. They are:

(1) whether there is a *benefit*;

(2) if so, whether the donor (or a person connected with the donor) *receives* that benefit; and

(3) if so, whether the donor (or the connected person) receives that benefit *in consequence of making the gift*.

It is convenient to consider each of these elements in turn.

Benefit

38. The principal argument advanced by Mr Goodfellow was that, since the effect of s 142 IHTA is to treat the varied dispositions, comprising the gifts to the charity, as taking effect for IHT purpose on the death of the testatrix, the effect is that no IHT liability in respect of those gifts ever arose. He submitted that it would be a misuse of language to describe someone as receiving a benefit in the form of a relief from a liability, which liability arises only if that person receives the benefit of certain property (and which liability is charged as a fraction of that property), where the liability is avoided by means of the person not receiving the benefit of the property. The associated liability is merely a feature or incident of receiving the benefit of the property; the benefit of the property has simply not been received and so the associated liability to IHT has not been incurred.

39. Mr Smith argued that s 142 creates a statutory fiction which is restricted to IHT. So pursuant to s 142 the will is treated as if it had been varied for the purposes of IHT. That creates the IHT exemption for the gifts to the Charity. One then disregards the statutory fiction for the purposes of income tax and looks at the reality. The reality is that the donor was entitled to the sum in question, which was re-directed to the Charity, but did not bear the liability that would but for the deed of variation have arisen.

40. We agree with Mr Smith. The effect of s 142 is confined to IHT, and has no deeming effect for the purpose of income tax, including therefore the relief under s 25 FA 1990. For income tax purposes the deed of variation operated solely as a direction from Mr Harris and Mrs Fine as residuary beneficiaries to the personal representatives to make the gifts to the Charity out of their respective shares of residue. For those purposes regard must be had to the fact of the putative liability to IHT that arose on the death of the testatrix, and the fact of its elimination by the deeming effect of the deed of variation. Accordingly, in line with the reality and not with the deemed IHT position, for income tax there was a liability to IHT, and it was subsequently removed. That in our view was a benefit. The property to which that liability would have attached, were it not to have been removed by the deed of variation, was property over which, for income tax purposes, Mr Harris and Mrs Fine had a right of disposition, and they exercised that right by means of the deed of variation.

41. Mr Goodfellow suggested that an analogy could be drawn between the effect of the variation and a discretionary bonus refused by an employee which, if received by him, would be taxable. The employee would not receive a benefit by reason of his not being subject to income tax in respect of the bonus he has not received. We do not consider this situation is analogous to the facts of this case. In the case of such an employee, for income tax purposes no tax liability has arisen at the time of his waiver, and accordingly no tax liability arises, or could arise, at all. This is because he has waived the receipt of what would otherwise be taxable remuneration. There could

only be a valid analogy with a waived discretionary bonus if Mr Harris and Mrs Fine had asked their mother in her lifetime to leave £500,000 in her will directly to the Charity, and not to them. That would have been a very different situation to that applicable in this case. By contrast here, as we have found, for income tax purposes an IHT liability did arise on the death of the testatrix, and it was then later eliminated by the deed of variation, and the residuary beneficiaries are to be regarded as having become entitled to the amounts subsequently gifted to the Charity. Whereas in the case of the waiver of a bonus there is no benefit of a reduction of tax, in the case of the deed of variation, for income tax purposes, there is in our view such a benefit.

Receives

42. Mr Goodfellow argued that the use of the word "receives" in s 25(2)(e) is deliberate and imports the concept of the prohibited benefit being provided to or accepted by the donor by or from another person. As such it is not apt to describe changes in the donor's fiscal position taking effect by operation of law without any provision of property by a third party. Mr Goodfellow submitted that this construction was consistent with what he argued was the perceived mischief of s 25(2)(e), namely to prevent the donor clawing back or securing from the charity or some other person a financial benefit in consequence of making the payment.

43. In support of his submissions, Mr Goodfellow argued that it was for this reason that the draftsman saw no need to include in s 25 an express exception from s 25(2)(e) for the financial advantages that the donor obtains by reason of the changes to the donor's taxation treatment in connection with making payments which would otherwise qualify as qualifying deductions. Those financial advantages would have been closely connected to the making of the qualifying payments and obvious to the draftsman. Mr Goodfellow referred us to four such advantages:

(1) Relief from higher rate income tax by reason of the extension of the basic rate band (s 25(6)).

(2) Reduction in the marginal rate of CGT by reason of the extension of the basic rate band (s 25(6)).

(3) Reduction in liability to interest on late paid income tax or CGT as a result of the reduction in liability to a principal amount of income tax or CGT (see s 86, Taxes Management Act 1970 – "TMA").

(4) Reduction in the donor's liability to default surcharge or tax-geared penalties as a result of the reduction in liability to principal amount of income tax or CGT (see ss 59C, 93(2) and 95(2) TMA).

44. All these financial advantages flow to the donor from the fact that the gift is a qualifying donation. The scheme of s 25 is to identify whether a gift is such a qualifying donation by reason, inter alia, of it satisfying the requirements of s 25(2), and then, in a case where the gift made by the donor in a year of assessment is a qualifying donation, to apply the Income Tax Acts and the TCGA in accordance with s 25(6) in order to provide the reliefs. It is evident therefore that the question whether a gift is a qualifying donation must be determined before, and accordingly without reference to the effect of, the operation of s 25(6). On this basis, none of the financial

advantages identified by Mr Goodfellow in this respect can be regarded as benefits for the purpose of s 25(2)(e).

45. Mr Goodfellow asked us to consider the position of a lifetime gift of cash to a charity to which the exemption from IHT under s 23 IHTA would apply. He submitted that, on the logic of HMRC's analysis, the IHT exemption would have been used to enable the donor to make a higher payment than he otherwise would have done, and the donor would thereby have enjoyed a prohibited benefit, either in the form of relief from IHT on what would otherwise have been an immediately chargeable lifetime transfer of value or in the form of increased relief from higher rate income tax.

46. We have answered this point in relation to the increased relief from higher rate tax. As regards the IHT exemption afforded on a lifetime gift to charity, this is in our view qualitatively different from a reduction in IHT by means of a deed of variation of a deceased's estate. In the latter case, as we have explained, a benefit arises for income tax purposes by the removal of the IHT liability that has arisen on death. In the former, by contrast, there never is such a liability requiring removal, and consequently the IHT exemption on a lifetime gift to charity is not a benefit within s 25(2)(e).

47. A similar analysis applies in our view to a further exemption to which Mr Goodfellow referred us. Section 587B, Taxes Act provides for income tax relief for non-arm's length disposals of qualifying investments to a charity. Such a disposal would also qualify for relief from CGT under s 257 TCGA, the effect under that provision being that the disposal is treated as taking place on a no gain, no loss basis, thus relieving the donor from CGT that would otherwise arise on a market value disposal (and preventing the creation of an allowable loss). Section 587B recognises that, in a case where a disposal by the charity itself might not be an exempt disposal, the effect of income tax relief for the donor could give rise to a double relief, and accordingly reduces the deemed acquisition cost of the asset in the charity by the amount (called "the relevant amount") for which income tax relief is given by s 587B(2) (see s 587B(4)).

48. Section 587B(5) contains restrictions on the relief where benefits are received by the person making the disposal or a connected person in consequence of making it. Unlike the position under s 25 FA 1990, this operates only as a reduction of the relevant amount on which income tax relief can be obtained, and not as a blanket disqualification. Mr Goodfellow argued in this connection that there was no question of the CGT relief under s 257 TCGA being a benefit to be taken into account as a reduction in the income tax relief. This was the case notwithstanding that if the donor had sold the qualifying investment and donated the proceeds to charity the CGT exemption would not have been available. Mr Smith argued that the application of both s 257 TCGA and s 587B, Taxes Act were no guide to the meaning of s 25 FA 1990, which related to gifts of cash and not to disposals of assets. It was unsurprising that reference had to be made to CGT in the case of disposals of qualifying investments.

49. In our view the answer to Mr Goodfellow's submission on the CGT relief afforded by s 257 TCGA is the same as our analysis of the IHT exemption under s 23 IHTA. Unlike the position where a deed of variation removes an IHT liability that had otherwise already arisen, no CGT will ever have been triggered on a gift of an asset to charity. There is therefore no benefit in the CGT exemption, and it does not alter that conclusion to point to another possible transaction that might have been entered into to crystallise a CGT liability, but was not.

50. Nor do we accept Mr Goodfellow's basic proposition on the construction of "receives" within s 25. In our view, "receives" is a neutral term, and does not import any requirement that the benefit must be provided to or accepted by the donor by or from another person. It looks solely to the position of the donor and asks the objective question whether any benefit has been received by the donor, without reference to the source of that benefit.

51. For the reasons explained earlier, we do not accept Mr Goodfellow's submissions on the mischief of s 25(2)(e), and we do not consider that reference to any of the non-statutory material before us can assist his arguments. Nor do we consider that the context of s 25 itself can restrict the meaning of s 25(2)(e). There is in our view no force in the argument that provisions concerning the right to receive benefits at intervals or the specific disregard of the benefit of a right of admission received in consequence of the making of the gift (ss 25(5A), and (5E) to (5G), inserted with effect for gifts made after 5 April 2000 by FA 2000) can in any way be regarded as indicative of, or as restricting, the meaning of s 25(2)(e).

52. We therefore conclude that Mr Harris and Mrs Fine each "received" the benefit of the IHT exemption in their capacity as residuary beneficiaries.

In consequence of making the gift

53. Mr Goodfellow argued that the gift is "the payment of a sum of money" to the Charity, and he referred in this respect to ss 25(1) and s 25(2)(a) FA 1990. He submitted that the gifts in question were not made until the sums were actually paid to the Charity. These payments were long after the reduction in the IHT liability had been achieved by the execution of the deed of variation and the making of the election under s 142 IHTA. The revised IHT treatment was not dependent on the actual making of the payments to the Charity. Absent some form of "sham" arrangement, if the executors had defaulted with the money or, due to a bank failure or fall in the value of the assets of the estate, those assets had been depleted, so that the payment to the Charity out of Mr Harris' or Mrs Fine's residuary entitlements was not or could not be made, the IHT treatment of the estate would have been the same.

54. Mr Goodfellow submitted further that the benefit of the reduction in IHT had been passed on fully to the Charity in the form of an increased cash payment. If a gift to the Charity had been chargeable to IHT the donors would have made their gifts subject to IHT. Accordingly, it was the Charity that had benefitted from the IHT exemption. In any event, he argued, how the donor funds the payment to charity (in particular the cost to the donor) is not relevant to whether the payment constitutes a qualifying payment.

55. As Mr Smith pointed out, the relevant causal connection in s 25(2)(e) is not between the benefit and the cash payment, but between the benefit and the making of the gift. It is true that one of the requirements of the section is that the gift must take the form of a sum of money, but the proper construction of s 25(2)(e) is that the benefit must be received in consequence of "the making of [the gift]". In our view that expression imports a wider meaning than the mere payment. Payment is the time when the gift is made, in the sense of having then been completed, but we consider that the expression "the making of the gift" encompasses not only that payment but the whole process whereby the gift is made and all the arrangements for the making of it. That would, as in this case, include the deed of variation under which Mr Harris and Mrs Fine directed the executors to make the cash payments to the Charity.

56. Certain of the situations envisaged by Mr Goodfellow in this connection, such as a fall in the value of certain classes of assets, would themselves have IHT consequences, and reduce the IHT payable on the estate. We do not need to concern ourselves with those details. We can agree with Mr Goodfellow's general proposition that that it cannot be said that the IHT saving was *dependent on* the gift to the Charity actually having been made by payment to the Charity, but this does not assist him; the test is not one of dependence but of consequence. The test is not whether the benefit is dependent on the gift having been made, but whether the benefit is in consequence of the making of the gift. That includes, as we have found, the arrangements or process whereby the gift is made.

57. Mr Goodfellow sought to rely upon s 25(12) FA 1990, which includes the definition of "relevant year of assessment" as meaning the year in which the gift is made. It was therefore clearly important, he said, to identify when the gift was made. This was the context in which s 25(2)(e) fell to be construed. We do not consider that this can assist the construction of s 25(2)(e). For the reasons we have given, in our view there is a clear distinction between consideration of the time when a gift is regarded as having been made (which is clearly relevant for determining the relevant year of assessment for which the reliefs are to be given) and the making of the gift, which is a wider expression and encompasses not only the concluding act whereby the gift is made, but also the process of the making of the gift and the associated arrangements whereby that is achieved. This, in our judgement, is the realistic view of the transaction and the way in which s 25(2)(e) is intended to apply to it.

58. Mr Smith sought to argue that a benefit would be in consequence of the making of a gift if it would not have arisen but for the gift. We do not accept this. The test is one of consequence which requires a different causal connection to a "but for" test. It is not in our view sufficient that a benefit would not have been received but for the making of the gift. The making of the gift (including, as we have found, the underlying arrangements whereby the gift is made) must be the reason why the benefit is received; it must in short be the cause of the benefit. Mr Smith sought to suggest further explanations of the meaning of "in consequence of", including that the benefit must be "integral to" the arrangements for the making of the gift, or by framing the question as: could the gift have been made other than with the benefit of the IHT saving? We do not consider that any further gloss is required to the plain

meaning of "in consequence of", which we regard as readily understandable on its own terms.

59. Viewed in this way we have no difficulty in concluding that the benefit of the reduction in the IHT liability was received by Mr Harris and Mrs Fine in consequence of the making of the gift to the Charity.

St Dunstan's

60. Mr Goodfellow criticised *St Dunstan's* and invited us not to follow it. We have, as we have indicated above, formed our own view of the construction of s 25(2)(e) having regard to the full arguments that have been advanced by the parties. In the event, on similar facts, we have reached the same conclusion as the Special Commissioner in that case. Mr Goodfellow's criticisms of that decision were essentially on grounds that he advanced in argument on this case before us, and which we have not accepted.

61. In his conclusion in *St Dunstan's* (at p 217), the Special Commissioner expressed himself thus:

> "In my opinion that benefit [of the IHT saving] arose 'in consequence of making [the gift] to St Dunstan's in the manner adopted by Mr Webber [the donor].' "

Whilst not expressed in the same way, we consider that the Special Commissioner's conclusion is consistent with our own finding that the making of the gift comprises not simply the payment to the Charity but all the arrangements for the making of the gift, including the deed of variation. Properly understood, we consider that this encompasses the reference by the Special Commissioner to "the manner adopted" by the donor in that case in making the gift.

Decision

62. We conclude therefore, for all the reasons we have given, that each of Mr Harris and Mrs Fine, as the donors, received a benefit in consequence of making the gift to the Charity. Since that benefit exceeded the de minimis amount provided by s 25(2)(e) FA 1990, the gift in each case does not satisfy the requirements of s 25(2), and consequently is not a qualifying donation.

63. Accordingly, we dismiss this appeal.

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

ROGER BERNER

TRIBUNAL JUDGE
RELEASE DATE: 18 August 2010