Neutral Citation Number: [2017] EWCA Civ 1512

Case No: A3/2015/3579

IN THE COURT OF APPEAL (CIVIL DIVISION)
ON APPEAL FROM THE HIGH COURT OF JUSTICE
CHANCERY DIVISION
MR JUSTICE MANN
[2015] EWHC 2878 (Ch)

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: 13/10/2017

Before:

LORD JUSTICE MCCOMBE
LORD JUSTICE SALES
and
LORD JUSTICE HENDERSON

- -

Between:

(1) BARCLAYS WEALTH TRUSTEES (JERSEY) LIMITED (2) MICHAEL DREELAN	**Appellants**
- and -	
THE COMMISSIONERS FOR HER MAJESTY'S REVENUE AND CUSTOMS	**Respondents**

- -

Mr David Ewart QC (instructed by **Forbes Hall LLP**) for the **Appellants**
Mr Rupert Baldry QC and Ms Sadiya Choudhury (instructed by **the General Counsel and Solicitor to HMRC**) for the **Respondents**

Hearing date: 24 May 2017

- -

Approved Judgment

Lord Justice Henderson:

Introduction

1. Chapter III of Part III of the Inheritance Tax Act 1984 ("IHTA" or "the 1984 Act") has applied since 22 March 2006 not only to settlements without interests in possession (of which discretionary trusts are the paradigm), but also to settlements in which interests in possession subsist which are not "qualifying interests in possession" as defined in section 59. Settled property in which no qualifying interest in possession subsists is defined in section 58(1) of IHTA as "relevant property", subject to certain exceptions which include, by virtue of section 58(1)(f), "excluded property". Before 22 March 2006, the scope of Chapter III of Part III was confined, broadly speaking, to discretionary trusts in which no interest in possession of any description subsisted.

2. Chapter II of Part III deals with interests in possession in settled property, although the scope of the Chapter was considerably curtailed in 2006 when settlements with non-qualifying interests in possession were, in effect, transferred to what had previously been the regime for all non-interest in possession trusts in Part III. The key concept which underpins Chapter II, and which dates back to the introduction of capital transfer tax by the Finance Act 1975 (see schedule 5 paragraph 3(1)), is the equation of beneficial entitlement to an interest in possession in settled property with beneficial entitlement to the property in which the interest subsists. This is now provided for by section 49(1) of the 1984 Act, which states 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."

In other words, a life or lesser interest in possession in settled property is equated with beneficial ownership of the underlying trust property itself.

3. By contrast, the taxation regime applicable to discretionary trusts and (since 2006) all other settled property in which no qualifying interest in possession subsists, although it has undergone various evolutions, has never sought to equate the interests of the beneficiaries with beneficial ownership of the whole or any specific part of the settled property. Instead, the general approach has been to impose a periodic charge to tax at 10-yearly intervals on property which remains in the settlement, and further charges to tax whenever property leaves the settlement (for example by distribution to a beneficiary) or otherwise ceases to be subject to the "relevant property" regime. It is convenient to refer to these two types of charge as "periodic" and "exit" charges respectively, although the latter term has never been used in the legislation itself. The rate of tax payable at each 10-year anniversary is normally 30% of the full rate payable on a lifetime chargeable transfer.

4. The present case concerns the first periodic charge which fell due on 21 June 2011 in respect of a Jersey-resident discretionary trust established by the settlor, Michael Dreelan, 10 years before on 21 June 2001 ("the 2001 Settlement"). By two notices of determination dated 23 April 2013 and addressed respectively to the trustee of the 2001 Settlement, Barclays Wealth Trustees (Jersey) Limited ("the Trustee"), and to

Mr Dreelan in his capacity as settlor of the 2001 Settlement, the Commissioners for Her Majesty's Revenue and Customs ("HMRC") determined that certain property comprised in the 2001 Settlement immediately before the 10-year anniversary, described in the notices as "the Qserv cash proceeds", was relevant property, and was not excluded property, with the consequence that a charge to tax arose in accordance with sections 64 and 66 of the 1984 Act.

5. Mr Dreelan and the Trustee (together "the taxpayers") appealed against the notices of determination, contending that the property in question was excluded property and therefore not subject to the periodic charge. On 25 November 2014, Peter Smith J made an order pursuant to IHTA section 222(3)(b) whereby he "notified" the appeals to the High Court, being satisfied "that the matters to be decided on the appeal are likely to be substantially confined to questions of law".

6. The hearing of the appeals took place before Mann J on 6 July 2015. The parties were represented by the same counsel as they have been before us, Mr David Ewart QC for the taxpayers, and Mr Rupert Baldry QC, leading Ms Sadiya Choudhury, for HMRC. By his reserved judgment and order dated 15 October 2015, the judge dismissed the taxpayers' appeals: see [2015] EWHC 2878 (Ch).

7. The taxpayers now appeal to this court, with permission granted by the judge. In his brief written reasons for granting permission, the judge described the matter as "a difficult one of statutory interpretation", and the result as "far from straightforward".

8. Before I set out the relevant facts, it will be helpful to give a brief description of the way in which the concept of excluded property operates in the IHT legislation, both in relation to property comprised in an individual's free estate and in relation to settled property.

Excluded property

9. By virtue of sections 1 and 2(1) of IHTA, tax is charged on the value transferred by "a chargeable transfer", which is a "transfer of value" made by an individual which is not an exempt transfer. Section 2(3) provides that references to chargeable transfers include references to occasions on which tax is chargeable under Chapter III of Part III, and thus include periodic and exit charges under the regime applicable to settled property in which there is no qualifying interest in possession.

10. Section 3 defines a transfer of value as a disposition as a result of which the value of the transferor's estate is reduced. Section 3(2) provides, however, that "no account shall be taken of the value of excluded property which ceases to form part of a person's estate as a result of a disposition".

11. Section 4(1) imposes a charge to tax on the death of a person as if, immediately before his death, he had made a transfer of value equal to the value of his estate at that time. Again, however, section 5(1)(b) provides that "the estate of a person immediately before his death does not include excluded property".

12. The basic definition of "excluded property" is contained in section 6(1), which states that:

> "Property situated outside the United Kingdom is excluded property if the person beneficially entitled to it is an individual domiciled outside the United Kingdom."

Two conditions therefore have to be satisfied if property comprised in an individual's free estate is to qualify as excluded property. The property in question must be situated outside the United Kingdom, and the beneficial owner of the property must be non-UK domiciled. A person's domicile is ascertained for this purpose in accordance with the general law, with the important exception that under section 267(1) a person not domiciled in the United Kingdom at any relevant time is treated for the purposes of the 1984 Act as domiciled in the United Kingdom (and not elsewhere) if:

> "…
>
> (b) he was resident in the United Kingdom in not less than 17 of the 20 years of assessment ending with the year of assessment in which the relevant time falls."

13. With regard to settled property, the basic provisions about excluded property are contained in section 48, which itself forms part of Chapter I of Part III. Section 48(1) deals with reversionary interests, and is not material for present purposes. Subsection (3) then states:

> "Where property comprised in a settlement is situated outside the United Kingdom –
>
> (a) the property (but not a reversionary interest in the property) is excluded property unless the settlor was domiciled in the United Kingdom at the time the settlement was made …"

It can be seen that this provision is analogous to section 6(1), in the sense that two similar conditions have to be satisfied if the settled property in question is to qualify as excluded property, one relating to the situs of the property and the other relating to the domicile of the settlor. It is important to note, however, that the domicile condition only has to be satisfied by the settlor "at the time the settlement was made". The effect of that requirement is one of the central issues arising on the appeal, but it is at least common ground that where a settlor makes a settlement of property situated outside the United Kingdom (which I will call "foreign property" for short) at a time when he is not UK-domiciled, and the property then remains comprised in the same settlement, its status as excluded property will not be lost merely because the settlor subsequently acquires an actual or deemed domicile in the United Kingdom.

14. Finally, section 82 contains a special rule which applies for the purposes of Chapter III only where property moves from one settlement to another. It needs to be read with section 81(1), which states that:

> "Where property which ceases to be comprised in one settlement becomes comprised in another then, unless in the meantime any person become beneficially entitled to the property (and not merely to an interest in possession in the

> property), it shall for the purposes of this Chapter be treated as remaining comprised in the first settlement."

Section 82 then provides, so far as material, as follows:

> "82 **Excluded Property**
>
> (1) For the purposes of this Chapter … property to which section … 81 above applies shall not be taken to be excluded property by virtue of section 48(3)(a) above unless the condition in subsection (3) below is satisfied (in addition to the conditions in section 48(3) that the property is situated outside the United Kingdom and that the settlor was not domiciled there when the settlement was made).
>
> (2) …
>
> (3) The condition referred to in subsections (1) and (2) above is –
>
> > (a)…
> >
> > (b) in the case of property to which subsection (1) … of section 81 above applies, that the person who is the settlor in relation to the second of the settlements mentioned in the subsection concerned,
>
> was not domiciled in the United Kingdom when that settlement was made."

15. The general effect of this additional requirement may be summarised as follows. Where property comprised in one settlement subject to Chapter III ("S1") is transferred to another such settlement ("S2"), the property in question, if it is to qualify as excluded property, must satisfy the further requirement that the settlor of S2 was non-UK domiciled when S2 was made.

16. With these statutory provisions in mind, I now turn to the facts.

The facts

17. On 21 June 2001, Mr Dreelan paid or transferred £100 to the Trustee (then called Walbrook Trustees (Jersey) Limited) to hold on the trusts of the 2001 Settlement. The trusts of the 2001 Settlement were in broad discretionary form, the main beneficiaries being Mr Dreelan himself, his spouse, and his children then living or born during a lengthy trust period. Further sums of cash were then settled by Mr Dreelan on 22 June and 27 July 2001, from bank deposits held by him personally in Jersey. At these dates, Mr Dreelan was not domiciled in the United Kingdom for inheritance tax purposes. His domicile under the general law was, and remains, in the Republic of Ireland.

18. The Trustee then lent part of the settled funds to a wholly-owned Jersey resident company called Minsk Limited ("Minsk"). At this stage, therefore, all the trust assets

(comprising the shares in Minsk, the loans to Minsk, and any uninvested cash held in Jersey) were excluded property by virtue of IHTA section 48(3).

19. On 4 February 2003, Mr Dreelan transferred 25,000 ordinary £1 shares in a UK-resident company, Qserv Limited ("Qserv"), to the Trustee, which in turn transferred them to Minsk. The Qserv shares, being property situated in the UK, were not excluded property during the brief period when they were held directly by the Trustee, but once they had been transferred to Minsk the whole of the trust fund was again excluded property, because the Qserv shares were held through Minsk the shares in which were excluded property in the hands of the Trustee.

20. In the tax years 2001/02 to 2007/08 inclusive, various distributions of excluded property were made to Mr Dreelan from the 2001 Settlement.

21. As from 6 April 2003, Mr Dreelan acquired a deemed domicile in the United Kingdom for IHT purposes under section 267 of the 1984 Act. This was based on his residence in Scotland for 17 of the preceding 20 years of assessment.

22. On 31 March 2008, Minsk was dissolved, and its assets, comprising the 25,000 ordinary £1 shares in Qserv and a portfolio of investments, were distributed to the Trustee as its sole shareholder. At this point, therefore, the Qserv shares were not excluded property because they were again directly owned by the Trustee.

23. On 4 April 2008, a new settlement was made by Mr Dreelan and his three brothers, Thomas, Sean and Ciaran. The settlement was called the Dreelan Brothers Joint Trust ("the DBJT"), and the Trustee was again the sole trustee. Each brother had an undivided non-qualifying interest in possession in one quarter of the trust fund, so the DBJT, like the 2001 Settlement, was subject to Chapter III of Part III of IHTA. On the same day, the Trustee, in exercise of its powers of appointment under the 2001 Settlement, appointed the 25,000 Qserv shares to be held for the benefit of Mr Dreelan on the trusts of the DBJT, freed and discharged from the trusts powers and provisions of the 2001 Settlement. Mr Dreelan also transferred a further 1,000 shares in Qserv which he owned personally to the DBJT. Following further share transfers from other Dreelan trusts and individuals, the DBJT owned on 4 April 2008 all 104,000 ordinary £1 shares in Qserv.

24. On 3 July 2008, the DBJT sold its Qserv shares for cash and an earn-out, the amount of which would be determined by Qserv's profits for the three years to 31 December 2010. It is common ground that the earn-out was property situated in the United Kingdom. One quarter of the assets arising from the sale of the Qserv shares (in the form of cash and entitlement to the earn-out), held by the Trustee in its capacity as trustee of the DBJT, therefore derived from the 26,000 shares transferred to it from the 2001 Settlement and by Mr Dreelan personally.

25. Various capital distributions (funded from the cash proceeds of the share sale) have been made from the DBJT to Mr Dreelan in the period from 3 July 2008 to date.

26. On 17 November 2009, Mr Dreelan's share of the capital of the DBJT (excluding the earn-out) was revocably appointed to a separate sub-fund in the DBJT to be known as Michael's Fund.

27. By a deed of appointment dated 2 June 2011 ("the 2011 Appointment"), the cash in Michael's Fund representing the original 25,000 Qserv shares which had been transferred from the 2001 Settlement (defined as "the Original Fund") and the further 1,000 Qserv shares which had been transferred into the DBJT by Mr Dreelan personally (defined as "the Added Fund") was irrevocably appointed by the Trustee back to the 2001 Settlement, to be held by the Trustee in its capacity as trustee of the 2001 Settlement "freed and released from the terms of the [*DBJT*] and Michael's Fund". The 2011 Appointment further provided that the Added Fund should be held separately from the rest of the trust fund of the 2001 Settlement. On the following day, the relevant funds were transferred from United Kingdom bank accounts of the DBJT to United Kingdom bank accounts of the 2001 Settlement, all held with Barclays Bank Plc.

28. On 16 June 2011, the Trustee transferred that cash into Jersey bank accounts where it remained until the 10-year anniversary date on 21 June 2011. Immediately before that date, therefore, the cash was foreign property. Furthermore, save in relation to the Added Fund, the cash represented the traceable proceeds of the original 25,000 Qserv shares which Mr Dreelan had added to the 2001 Settlement in February 2003, at a time when he was still non-UK domiciled.

Settlements and settled property: relevant definitions in the 1984 Act

29. In order to complete the statutory picture, it is necessary to refer to some key definitions in Chapter I of Part III of the 1984 Act.

30. "Settlement" is defined in section 43, as follows:

> "43 **Settlement and related expressions**
>
> (1) The following provisions of this section apply for determining what is to be taken for the purposes of this Act to be a settlement, and what property is, accordingly, referred to as property comprised in a settlement or as settled property.
>
> (2) "Settlement" means any disposition or dispositions of property, whether effected by instrument, by parol or by operation of law, or partly in one way and partly in another, whereby the property is for the time being –
>
> (a) held in trust for persons in succession or for any person subject to a contingency, or
>
> (b) held by trustees on trust to accumulate the whole or part of any income of the property or with power to make payments out of that income at the discretion of the trustees or some other person, with or without power to accumulate surplus income, or
>
> (c) …,

> or would be so held … if the disposition or dispositions were regulated by the law of any part of the United Kingdom; or whereby, under the law of any other country, the administration of the property is for the time being governed by provisions equivalent in effect to those which would apply if the property were so held ..."

31. The definition of "settlement" therefore requires a combination of two things: first, a disposition or dispositions of property, and secondly, a state of affairs brought about by that disposition or those dispositions, whereby the property is held in various ways, or would be so held if the conditions at the end of subsection (2) were satisfied. In broad terms, paragraph (a) of subsection (2) covers fixed-interest trusts, such as those in the DBJT, while paragraph (b) covers discretionary trusts, such as those of the 2001 Settlement. Both the DBJT and the 2001 Settlement were governed by Jersey law, but the hypotheses relating to foreign law at the end of the subsection clearly bring them within the scope of the definition.

32. Section 44 then defines "settlor", as follows:

> "44 **Settlor**
>
> (1) In this Act "settlor", in relation to a settlement, includes any person by whom the settlement was made directly or indirectly, and in particular (but without prejudice to the generality of the preceding words) includes any person who has provided funds directly or indirectly for the purpose of or in connection with the settlement or has made with any other person a reciprocal arrangement for that other person to make the settlement.
>
> (2) Where more than one person is a settlor in relation to a settlement and the circumstances so require, this Part of this Act … shall have effect in relation to it as if the settled property were comprised in separate settlements."

33. It is also relevant to note the following provisions in Chapter III, apart from those which I have already mentioned:

> "60 **Commencement of settlement**
>
> In this Chapter references to the commencement of a settlement are references to the time when property first becomes comprised in it.
>
> 61 **Ten-year anniversary**
>
> (1) In this Chapter "ten-year anniversary" in relation to a settlement means the tenth anniversary of the date on which the settlement commenced and subsequent anniversaries at ten-yearly intervals …
>
> …

> 64 **Charge at ten-year anniversary**
>
> (1) Where immediately before a ten-year anniversary all or any part of the property comprised in a settlement is relevant property, tax shall be charged at the rate applicable under sections 66 and 67 below on the value of the property or part at that time.
>
> …
>
> 65 **Charge at other times**
>
> (1) There shall be a charge to tax under this section –
>
>> (a) where the property comprised in a settlement or any part of that property ceases to be relevant property (whether because it ceases to be comprised in the settlement or otherwise); …
>>
>> …
>
> (7) Tax shall not be charged under this section by reason only that property comprised in a settlement ceases to be situated in the United Kingdom and thereby becomes excluded property by virtue of section 48(3)(a) above.
>
> …"

34. The provisions of sections 60 and 61(1) explain why the first periodic charge in relation to the 2001 Settlement occurred on the tenth anniversary of the date when it was originally made, even though only £100 was then settled. Section 64(1) shows that the charge is on the "relevant property" comprised in the 2001 Settlement immediately before the ten-year anniversary, regardless of whether the settled property was relevant property at any earlier times; if it was not, appropriate adjustments are however made to the rate of charge under section 66(2). Section 65(1)(a) is the basic provision which imposes an exit charge when settled property ceases to be relevant property, but by virtue of subsection (7) there is no charge to tax merely because settled property becomes excluded property under section 48(3)(a) by being removed from the United Kingdom. Thus, for example, no exit charge would have been triggered when the Trustee transferred the cash subject to the 2011 Appointment from United Kingdom to Jersey bank accounts on 16 June 2011, a few days before the ten-year anniversary, on the assumption that the cash then became excluded property.

35. In Rysaffe Trustee Co (CI) v IRC [2002] EWHC 1114 (Ch), [2002] STC 872, Park J made the important point, with which I respectfully agree, that the provisions of the 1984 Act relating to settlements are, in the absence of special provision, for the most part left to be interpreted in accordance with the general understanding of trust practitioners: see his judgment at [18] to [21]. The particular issue in that case was whether the settlor had made five separate discretionary settlements by executing five separate trust instruments, or whether he should be treated as having made a single

settlement. After pointing out at [18] that the decision whether to make a single settlement, or several settlements, or to add property to an existing settlement, is one for the settlor to take, Park J continued:

> "19. Examples of the sort in the previous paragraph can be multiplied many times over. They show that it is not necessary to have a statutory definition to determine whether there is one settlement or more, and if more than one, how many. Trust practitioners can recognise a separate settlement when they see one, and equally they can recognise a case where there is only one settlement, not several settlements, when that is what they see. Often, fiscal considerations apart, it will make little or no difference in the end whether, for example, a settlor chooses to make one large settlement, or instead to make several smaller settlements. But there is no doubt that as a matter of general principle the two courses are different and create analytically different structures. What kind of structure a particular settlor has created will depend on how he chooses to do it.
>
> 20. All of that assumes no detailed statutory definition. However, the Inheritance Tax Act 1984 has s 43, which begins by saying that the provisions of the section "apply for determining what is to be taken for the purposes of this Act to be a settlement". Notwithstanding those words of the statute, my opinion is that s 43 gives little or no guidance to answering the question of whether, in the many permutations of circumstances of which I gave a few illustrations in [18] above, there is one settlement or more than one. In my judgment the draftsman has for the most part left those questions to be answered in accordance with general principles – in accordance with what I have described above as the general understanding of trust practitioners."

Applying this approach, Park J held that there were no grounds on which to go behind the settlor's choice to execute five separate settlements, each of which had a separate identity for IHT purposes: see the summary of his conclusions at [17].

36. The approach and reasoning of Park J in the Rysaffe case were approved on appeal to this court: see [2003] EWCA Civ 356, [2003] STC 536, at [25] to [26] per Mummery LJ, with whom Dyson and Schiemann LJJ agreed.

The issues

37. Now that I have set the scene, I can return to the basic issue. The question which divides the parties is whether the money held by the Trustee in Jersey bank accounts immediately before the ten-year anniversary of the 2001 Settlement on 21 June 2011, and which represented in part the Trustee's original holding of 25,000 Qserv shares, was or was not excluded property.

38. If the 25,000 Qserv shares (and the proceeds of their later disposal) had throughout remained in the 2001 Settlement, there could be no real doubt about the answer to this

question. The conditions in section 48(3) of the 2004 Act would clearly be satisfied, because:

(a) the cash which represented the shares on 20 June 2011, immediately before the anniversary date, was foreign property;

(b) Mr Dreelan was not UK-domiciled when the 2001 Settlement was first established by him on 21 June 2001; and (if it matters)

(c) he was also not UK-domiciled when he transferred the 25,000 shares to the 2001 Settlement in February 2003. Accordingly, even if the addition of the shares were properly to be regarded as the making by him of a fresh settlement within the meaning of section 43, of which he was the settlor pursuant to section 44, the "settlor" condition in section 48(3) would nevertheless still be satisfied.

39. The difficulty is caused by the involvement of the DBJT, to which the Qserv shares were appointed on 4 April 2008 and from which part of the proceeds of sale of the shares was appointed back to the 2001 Settlement by the 2011 Appointment. These transactions engage the special deeming provision in section 81(1), which applies where property moves between settlements. The transactions also require consideration of the special excluded property rule in section 82(1) and (3), whereby property to which section 81 applies cannot be excluded property unless (in addition to the usual conditions in section 48(3)) the relevant settlor (here Mr Dreelan) was non-UK domiciled when the second settlement was made. Since Mr Dreelan had a deemed UK domicile at that date, it follows that the property settled by him on the trusts of the DBJT (whether indirectly by means of the April 2008 appointment from the 2001 Settlement, or directly by his transfer of 1,000 Qserv shares to the Trustee) could never qualify as excluded property while it remained property to which section 81 applied. Finally, consideration has to be given to the 2011 Appointment itself, and the question whether it independently constituted the making of a further settlement by Mr Dreelan on that date. If it did, he was clearly UK-domiciled when that further settlement was made.

Discussion

40. In considering these issues, I will begin with the effect of the deeming provision in section 81(1). For convenience, I will set it out again:

> "Where property which ceases to be comprised in one settlement becomes comprised in another then, unless in the meantime any person becomes beneficially entitled to the property (and not merely to an interest in possession in the property), it shall for the purposes of this Chapter be treated as remaining comprised in the first settlement."

41. There can be no doubt that, when the 25,000 Qserv shares were appointed by the Trustee on 4 April 2008 from the 2001 Settlement to the DBJT, they ceased to be comprised in the former settlement and became comprised in the latter. The appointment expressly stated that the shares were to be held "upon the trusts and subject to the powers and provisions of [*the DBJT*] and discharged from the trusts, powers and provisions of [the 2001 Settlement]." Nor was there any intermediate

stage when Mr Dreelan (or anybody else) became beneficially entitled to the shares. Accordingly, section 81(1) applied with the consequence that, for the purposes of Chapter III, the shares had to be treated as remaining comprised in the 2001 Settlement for so long as they (or, after the sale, their proceeds) were in fact comprised in the DBJT.

42. The next point to make is that the purposes of Chapter III clearly include the periodic charge to tax on the first ten-year anniversary of the 2001 Settlement.

43. Since the shares (and, after the sale, their proceeds) are deemed to have remained throughout in the 2001 Settlement, it must in my judgment further follow (again for the purposes of Chapter III) that the 2011 Appointment did not itself engage section 81, although in reality the property subject to the 2011 Appointment ceased to be comprised in the DBJT and became comprised in the 2001 Settlement. Because the property appointed back to the 2001 Settlement was already conclusively deemed to be comprised in it, by the prior application of Section 81(1), there could be no scope for the section to apply again so as to deem the appointed property to remain in the DBJT.

44. It is also clear that, while the shares and their proceeds remained in the DBJT, they were not excluded property. There were two separate reasons for this. First, neither the shares nor the cash proceeds of sale held in UK bank accounts were foreign property. Secondly, the settlor, Mr Dreelan, was UK-domiciled when the DBJT was made, so the further condition in section 82(3) could not be satisfied.

45. Thus far, I believe that my analysis is uncontroversial. The next step in the analysis, as I see it, is that once the 2011 Appointment had been made and implemented, the deeming effect of section 81(1) in relation to the property restored to the 2001 Settlement was spent, and it was no longer "property to which section … 81 … applies" for the purposes of section 82(1). There was no need to deem the cash derived from the sale of the shares to be comprised in the 2001 Settlement, since that was now the reality. It further follows, in my judgment, that the question whether the cash (once it had been transformed into foreign property by transfer to Jersey bank accounts on 16 June 2011) was then excluded property must depend on section 48(3), and the answer to the question when "the settlement was made" within the meaning of subsection (3)(a).

46. It is at this point that the arguments of the parties diverge. On behalf of the taxpayers, Mr Ewart QC submits that the position is straightforward. The settlement in which the property was comprised can only be the 2001 Settlement, and it was made on 21 June 2001 when Mr Dreelan was non-UK domiciled. That is how any trust practitioner would view the matter, and on the authority of Rysaffe that is the correct approach to adopt. Mr Ewart goes on to submit that the 2011 Appointment cannot be regarded as a "disposition … of property" within the definition of "settlement" in section 43(2), because the appointed property was already conclusively deemed by section 81(1) to be comprised in the 2001 Settlement when the 2011 Appointment was executed. If the property already formed part of the 2001 Settlement, it could not simultaneously be the subject of a disposition settling it on the trusts of the 2001 Settlement. That would be to contradict the clear consequences of the statutory deeming.

47. In support of his submissions on the correct approach to the interpretation of statutory deeming provisions, Mr Ewart referred us to the well known statement by Peter Gibson J, sitting in this court with Balcombe and Simon Brown LJJ, in Marshall (Inspector of Taxes) v Kerr [1993] STC 360 at 366:

> "For my part I take the correct approach in construing a deeming provision to be to give the words used their ordinary and natural meaning, consistent so far as possible with the policy of the Act and the purposes of the provisions so far as such policy and purposes can be ascertained; but if such construction would lead to injustice or absurdity, the application of the statutory fiction should be limited to the extent needed to avoid such injustice or absurdity, unless such application would clearly be within the purposes of the fiction. I further bear in mind that because one must treat as real that which is only deemed to be so, one must treat as real the consequences and incidents inevitably flowing from or accompanying that deemed state of affairs, unless prohibited from doing so."

This statement of principle has been cited with approval in many subsequent cases, including DV3 RS Ltd Partnership v Revenue and Customs Commissioners [2013] EWCA Civ 907, [2013] STC 2150, at [13] and [14] per Lewison LJ, with whom Gloster and Maurice Kay LJJ agreed. Lewison LJ added, at [15], that the fact that deeming provisions are involved "does not displace the ordinary principles of statutory interpretation".

48. On behalf of HMRC, Mr Baldry QC seeks to place the issue in the wider context of the scheme of the IHT legislation as it applies to excluded property. The general rule is that foreign property owned by a non-UK domiciled person is outside the scope of the tax, but if that person subsequently becomes UK-domiciled (including by acquisition of a deemed UK domicile under section 267) all his non-settled foreign property immediately ceases to be excluded property within the meaning of section 6 and so falls within the scope of IHT. If he were then to transfer the foreign property into a settlement, this would give rise to a chargeable transfer and the settled property would not be excluded property within section 48(3). Thus, once an individual has become UK-domiciled, the legislation does not permit him to take assets out of the scope of IHT by settling them offshore. Similarly, the basic purpose of section 81 is to prevent avoidance of the periodic charge by treating settled property transferred to another settlement as remaining in the original settlement. However, this purpose does not extend to deeming excluded property to retain that status if it is transferred to a settlement created by a UK-domiciled settlor: see section 82(3)(b). Against this background, says Mr Baldry, it would be inconsistent with the scheme of the legislation if it were construed as permitting a settlor in Mr Dreelan's position to settle assets after becoming UK-domiciled in such a way that they became excluded property.

49. Mr Baldry goes on to submit that, when the property was transferred back to the 2001 Settlement as a result of the 2011 Appointment, the transfer was a non-event for the purposes of section 81, because the property was deemed to have remained in the 2001 Settlement throughout, and section 81 therefore continued to apply to the

property after it reverted to the 2001 Settlement. If that is right, section 82 remained in play, and Mr Dreelan remained unable to satisfy the condition in section 82(3)(b).

50. Mr Baldry further submits that, with its focus on dispositions, the definition of "settlement" in section 43 leads to the conclusion that a separate settlement is created for IHT purposes whenever a settlor adds property to an existing settlement. Thus he did not shrink from submitting that in 2001 Mr Dreelan made three separate settlements for IHT purposes when he settled the original £100 on the trusts of the 2001 Settlement and then made two further transfers of property to it, even though any trust lawyer would say that Mr Dreelan had made a single settlement and then added property to it. With regard to section 48(3), he submits that the time when "the settlement was made" must refer to each act of settling property by a disposition, even though the opening words of the subsection ("Where property comprised in a settlement is situated outside the United Kingdom") are naturally read as referring to the ongoing settlement as it exists from time to time and as a trust lawyer would identify it, rather than to each dispositive act by which it was constituted. On the correct purposive approach, he submits, the court should not be reluctant to construe the word "settlement" as having two different meanings within section 48(3), although if necessary he would adopt the preferred view of the judge at [28] that both references to "settlement" in the subsection are to the individual dispositive acts whereby property is settled.

51. In my judgment, the submissions for the taxpayers are correct and the property in question was indeed excluded property immediately before the ten-year anniversary on 21 June 2011. My main reasons for reaching this conclusion are as follows.

52. First, I consider the better view to be that the 2001 Settlement was a single settlement for IHT purposes, constituted by a number of separate dispositions of property to be held on the trusts thereof. Those dispositions included the three transfers to the Trustee made by Mr Dreelan in 2001, his transfer of the 25,000 Qserv shares to the Trustee on 4 February 2003, and the transfer effected by the 2011 Appointment. Not only is this how a trust lawyer or practitioner would view the matter, but it fits comfortably with the definition of "settlement" in section 43(2) which applies for all purposes of the 1984 Act. In particular, the express reference to "disposition or dispositions of property" in the definition is in my view naturally read as intended to cover the common situation where a settlement is first made, often with a small or nominal sum of money, and further assets are then added by the settlor. This was rightly recognised by Park J in Rysaffe at [21], where he said:

> "Let me consider the implications of the plural "dispositions". In my view the use of the plural is merely a recognition that in a case where there is a settlement (i.e. only one settlement) it is possible for there to have been more dispositions to the trustees than one. A typical case is where a settlor creates his settlement with one disposition, and later adds more property to it by one or more other dispositions."

53. Secondly, I find it implausible to suppose that in section 48(3) the same word "settlement" was intended by Parliament to have two different meanings, or that it has a single meaning which requires one to focus separately on each occasion when property is added to a settlement. At least in cases of the type which I have described,

the natural (and in my opinion correct) interpretation of the subsection is that it requires one to look at a single settlement as it is constituted from time to time, whether by one or a series of transfers into settlement, and provides that any foreign property comprised in it is excluded property unless the settlor was UK-domiciled "at the time the settlement was made". The time when the settlement was made will then be ascertained in accordance with the usual principles of trust law, and will normally be the occasion when the settlor first executed a trust instrument and constituted the trust by providing property to the trustee.

54. In the present case, there can be no doubt that the 2001 Settlement was made by Mr Dreelan on 21 June 2001. Using time-honoured language, the trust instrument begins with the words "This instrument of trust is made 21st June 2001 …". It then recited the desire of the settlor to make the trust, and the fact that he had paid or transferred to the Original Trustees the property specified in clause C1, namely £100, "to the intent that they should hold it upon the trusts and in the manner declared in this instrument". The definition of the "Trust Fund", which was in standard form, included "all other money investments or other property" which might subsequently be transferred or paid to the Trustees and accepted by them as additions to the fund, together with the property from time to time representing the same.

55. Thirdly, I do not think it makes any difference that the Qserv shares (which were never foreign property) were appointed from the 2001 Settlement to the DBJT, and the cash proceeds of their sale were later appointed back to the 2001 Settlement by the 2011 Appointment. These transactions engaged section 81 of the 1984 Act, but as I have already explained the effect of section 81(1) was to deem the shares and their proceeds to remain comprised in the 2001 Settlement. The force of that deeming was in my view spent, in relation to the property appointed back to the 2001 Settlement, once the 2011 Appointment had been executed and the consequential transfers effected. I cannot accept Mr Baldry's submission that the property in question somehow remained property to which section 81 applied, within the meaning of section 82(1), once those steps had been taken.

56. Fourthly, even if it were somehow possible to regard the 2011 Appointment as effecting a separate settlement within the meaning of section 43, I would accept the submissions of Mr Ewart that for the purposes of Chapter III of Part III, including in particular the periodic charge to tax, such an analysis is precluded by the deeming provision in section 81(1). Since the property subject to the 2011 Appointment is conclusively deemed to have remained throughout in the 2001 Settlement, it cannot consistently with that deeming be treated as the subject of a separate disposition into the 2001 Settlement at the same time. Furthermore, the purposes of Chapter III include the question whether the property subject to the 2011 Appointment became excluded property in the 2001 Settlement, because the periodic charge to tax under section 64 is on "relevant property", and "relevant property" is defined in section 58(1)(f) as not including "excluded property".

57. Finally, I do not see anything at all surprising or anomalous in reaching the conclusion that the property representing the 25,000 Qserv shares in the 2001 Settlement at the date of the periodic charge was excluded property. As I have already pointed out, the Qserv shares were transferred to the Trustee at a time when Mr Dreelan was still non-UK domiciled, and if they had never left the 2001 Settlement their proceeds, if invested as foreign property, would undoubtedly have

qualified as excluded property. I can see no mischief which might require the language of the 1984 Act to be interpreted so as to produce the opposite conclusion merely because there was an intermediate transfer of the Qserv shares between the two settlements. The facts of the present case are highly unusual, and there is no suggestion that they formed part of any scheme of tax avoidance. The consequences within Part III of a transfer of property between settlements are dealt with by section 81, and I see no occasion to strain the language of that section, or of section 48, in order to reach a different conclusion in this case.

58. For completeness, I should mention that different considerations may arise in cases where a settlor makes an offshore settlement when he is non-UK domiciled, later acquires a UK domicile, and then makes further substantial transfers of property into the settlement. It may arguably seem anomalous that, in such a case, the property in question, if it is or becomes foreign property, should qualify as excluded property in the settlement merely because the settlor was non-UK domiciled when the settlement was originally made. I emphasise that the present case is not of that character, because the Qserv shares originated in the 2001 Settlement, and were transferred to it at a time when Mr Dreelan was non-UK domiciled. I express no view on the question whether the same result as in the present case should be reached in cases of the other type which I have described, because wider policy considerations may then be engaged. For similar reasons, I prefer to express no view on some of the wider arguments which were addressed to us but are unnecessary for the resolution of this case.

The judgment of the judge

59. I have so far made almost no reference to the judgment below, in which the judge explained why he found in favour of HMRC. That is not out of any discourtesy to a judge for whom I have the greatest respect, but merely reflects the fact that, on a difficult question of construction of this nature, I find it preferable to start from first principles and the arguments addressed to us in this court, rather than discussing the case through the prism of the judgment below. I will, however, briefly address some of the key points which found favour with the judge.

60. The judge discussed the statutory definition of "settlement", and the question when a settlement is "made", in his judgment at [20] to [32]. There is much that I agree with in these paragraphs, but I cannot accept the judge's view that the word "settlement" may have two different meanings in section 48(3), or that the 2011 Appointment involved the making of a separate settlement of the appointed property by Mr Dreelan. I also respectfully think that the judge was over-influenced by policy considerations which do not arise on the facts of the present case: see in particular his judgment at [31] and [32].

61. The judge then considered the deeming effect of section 81 at [33] to [37]. He rejected Mr Ewart's submission, which I have accepted, to the effect that it would contradict the deeming required by section 81 if the 2011 Appointment were regarded as the making of a new settlement by Mr Dreelan. The judge thought that Mr Ewart's submission would result in section 81 operating outside the scope of Chapter III, and that it should not influence the construction of section 48 which is in Chapter II: see [37]. I do not agree, because (as the judge rightly recognised) the concept of "excluded property" is deployed within Chapter III, by virtue of section 58(1)(f), and

its meaning in that context must in my view take account of the deeming required by section 81.

62. The judge then returned to the true construction of section 48(3), in a passage which I will quote in full:

> "39. … The true construction of section 48(3) is one that requires one to look at the occasion of the settling of the property for the purposes of determining whether or not it is excluded property, and nothing else. It does not create a separate settlement for the other purposes of the Act, deemed or otherwise. The overall settlement for the purposes of section 64 remains the same. *Rysaffe* enables (and requires) one to look at basic trust law for determining that. [*The judge then referred to sections 64, 61 and 60 of IHTA*].
>
> 40. All those are (in the circumstances) references to the [*2001 Settlement*], implicitly acknowledging that property may have arrived in it at different times. That is what has happened here. The correct interpretation of section 48(3) has no impact on this. It involves considering the circumstances of the settlement of property at one point in time, and does not otherwise involve the creation of any "settlement" which differs from the overall [*2001 Settlement*].
>
> 41. Nor does *Rysaffe* itself compel a contrary conclusion on section 48(3). That case determines that the concept of what is a settlement, for the purposes of the provisions of the Act considered by Park J, is the same as that understood by the general law. Thus in his case there were 5 real world settlements, and not one, and therefore there were 5 settlements for the purposes of the Act. Park J was not considering every reference to the word "settlement" in the Act, and was not considering the detail of what was the making of the settlement for the purposes of section 48(3)(a). I therefore consider that *Rysaffe* does not assist Mr Ewart."

63. This passage clearly explains the judge's thinking, but in my view it is open to the criticism that it favours a construction of section 48(3) which is at odds with the normal conception of what constitutes a settlement, even though (as the judge recognised) that normal conception is reflected elsewhere in the 1984 Act, and notably in section 64 itself. For my part, I prefer to construe section 48(3) in a way that accords as far as possible with the usual practice and understanding of trust lawyers and practitioners; and in the context of the present case, such an approach seems to me to provide strong support for Mr Ewart's submissions.

Conclusion

64. For the reasons which I have given, I would allow the taxpayers' appeal.

Lord Justice Sales:

65. I agree.

Lord Justice McCombe:

66. I also agree.