[2013] UKFTT 436 (TC)

TC02830

Appeal numbers: TC/2011/4717 & TC/2011/8729

Income tax – trust – copyright royalties – direction not to distribute as income – whether accumulation of income – whether taxable at the rate applicable to trusts – Income and Corporation Taxes Act 1988, s 686 – whether taxable at the trust rate – Income Tax Act 2007, s 479

FIRST-TIER TRIBUNAL
TAX CHAMBER

THE TRUSTEES OF THE MRS PL TRAVERS WILL TRUST — **Appellants**

- and -

THE COMMISSIONERS FOR HER MAJESTY'S REVENUE & CUSTOMS — **Respondents**

TRIBUNAL: JUDGE NICHOLAS PAINES QC
JUDGE JILL GORT

Sitting in public at 45 Bedford Square, London WC1 on 17 and 18 April 2013

Mr Michael Furness QC, instructed by Goodman Derrick LLP, for the Appellant

Mr David Yates of Counsel, instructed by the General Counsel and Solicitor to HM Revenue and Customs, for the Respondents

DECISION

1. Mary Poppins, the children's nanny with magical powers who appears and disappears mysteriously in the lives of the Banks family of Cherry Tree Lane, is an enduringly popular figure in children's literature. She owes her popularity to a film produced by Walt Disney in the 1960s and a stage musical produced by Sir Cameron Mackintosh in 2004, but first of all to a set of children's books written by Pamela Lyndon Travers – or PL Travers, as she styled herself on the title pages – over a period of nearly fifty years commencing in the 1930s. The issues we have to decide relate to the tax treatment, in the tax years from 2004-05 to 2008-09, of royalties from the stage musical in the hands of the trustees of PL Travers' will trust. For the reasons we give in the Decision, we have concluded that those royalties were taxable at the higher rate applicable to trust income by virtue of the relevant income tax legislation insofar as they derived from an exclusive copyright licence granted by PL Travers to Cameron Mackintosh Ltd (hereafter 'CML') but not insofar as they derived from a later assignment of the relevant copyright. In order to decide this appeal we have had to decide a point of interpretation of a now repealed provision of the Law of Property Act 1925 which appears not to have been the subject of a judicial decision in more than two centuries of the provision's existence.

2. The issue arises in the following way. In 1994 PL Travers made an agreement with CML and another company with a view to the writing and production of a stage musical about Mary Poppins; this was subject to the consent of Walt Disney Productions because of a term of an agreement in 1960 relating to the Walt Disney film. Owing to a failure to reach agreement with Walt Disney Productions, the stage musical was not produced until 2004, after the trustees had intervened to break a deadlock between CML and Walt Disney. In the meantime PL Travers had died (aged 96 years) in April 1996, leaving a will which settled her literary estate upon a settlement, the beneficiaries of which were PL Travers' descendants and the Cherry Tree Foundation, a charity set up by her. Under the terms of the settlement the trustees were to pay out the income of the settlement to the beneficiaries for 80 years, at the end of which they were to distribute the capital among certain of the descendants of PL Travers alive at the time.

3. The stage musical *Mary Poppins* opened in the West End of London at the end of 2004. The trustees took the view that the trust's receipts in respect of the musical (which we shall call 'the CML royalties') were capital and not income of the trust, and therefore were not to be distributed but preserved for 80 years. They also took the view that the CML royalties were liable to income tax at the basic rate only because they were not caught by section 686 of the Income and Corporation Taxes Act 1988 ('ICTA 1988'). They prepared the trust's tax returns accordingly. A note was included in a box in the returns (the 'white space') disclosing what had been done. In 2007 and subsequently, HMRC enquired into the returns and concluded that the

payments were subject to tax at the higher rate applying to trusts by virtue of s 686 of ICTA 1988 or s 479 of the Income Tax Act 2007 which had replaced s 686. This appeal is against the decisions to that effect in respect of the tax years under appeal.

The tax legislation

4. Section 686 of ICTA 1988 governed the first four years of assessment under appeal. It provided, so far as material, as follows:

> **686 Accumulation and discretionary trusts: special rates of tax**
>
> (1) So far as income arising to the trustees of a settlement is income to which this section applies it shall … be chargeable to income tax at the rate applicable in accordance with subsection (1AA) below, instead of at the basic rate ….
>
> (1AA) The rate applicable in accordance with this subsection is—
>
> …
>
> (b) in the case of any other income to which this section applies, the rate applicable to trusts.
>
> (2) This section applies to income arising to the trustees of a settlement in any year of assessment so far as it—
>
> (a) is income which is to be accumulated or which is payable at the discretion of the trustees or any other person (whether or not the trustees have power to accumulate it) ....

5. Sections 479 and 480 of the 2007 Act applied in the final year under appeal. Their relevant provisions are materially the same as those of s 686, but differently arranged. They provide

> **479 Trustees' accumulated or discretionary income to be charged at special rates**
>
> (1) This section applies if –
>
> (a) accumulated or discretionary income arises to the trustees of a settlement ....
>
> (2) Income tax is charged on the income at the rates referred to in this section instead of the rates which would otherwise apply ....
>
> (3) Income tax is charged on the income at the dividend trust rate so far as income is dividend income.

(4) Otherwise, income tax is charged on the income at the trust rate ....

480 Meaning of "accumulated or discretionary income"

(1) Income is accumulated or discretionary income so far as –

(a) it must be accumulated, or

(b) it is payable at the discretion of the trustees or any other person,

and it is not excluded by subsection (3).

6. The provisions catch income in two categories of case: where it is to be accumulated and where it is payable at the trustees' discretion. The issue in this case is whether the CML royalties are income that is to be accumulated. It was common ground between the parties that the decision of the Court of Appeal in *Howell v Trippier* [2004] EWCA Civ 885 [2004] STC 1245 is authority that the expression 'income which is to be accumulated or is payable at the discretion of the trustees' in s 686(2)(a) of ICTA 1988 refers to receipts which are treated as income for the purposes of the law of trusts. The word 'income' thus has a different meaning in sub-s (2)(a) from the meaning it has in the expression 'income arising to the trustees' in the opening words of sub-s (1) and sub-s (2). In that expression it means income which the tax legislation regards as income and it is common ground that the royalties are such income, taxable at least at the basic rate.

7. Nobody suggested that the corresponding provisions in the 2007 Act were to be interpreted differently. We therefore interpret section 480(1) in accordance with *Howell v Trippier*; we do not consider that Parliament (which must be taken to have been aware of *Howell v Trippier*) can have intended, in re-writing section 686, to alter its meaning. We add for completeness that it was not suggested that the royalties are excluded by s 480(3).

The issues in outline

8. The parties disagree as to whether the royalties are receipts which the law of trusts regards as income; they also disagree as to whether, if they are income, the manner in which the trustees are directed to deal with them amounts in the circumstances to effecting an accumulation of income.

9. For the trustees Mr Michael Furness QC submits that the CML royalties are not income in trust law terms; this is for one or both of two reasons: (a) because such receipts have been held to be capital receipts for trust law purposes or (b) because PL Travers' will directs the trustees to treat them as capital, something which case-law indicates that a settlor is empowered to do. Alternatively, he submits, even if the

receipts are income, the manner in which the trustees are required to deal with them does not amount to accumulating them in the trust law sense because the copyrights, having a limited life, are wasting assets and the building up of a fund (even if built up from income) to replace a wasting asset does not amount to an accumulation.

10. In this connection there is a dispute about whether the CML royalties derive from the 1994 agreement, made by PL Travers in her lifetime, or from an agreement which is expressed as amending the 1994 agreement but was relied on as the effective source of the receipts; this was an agreement between the trustees and CML made in 2004 in parallel with an agreement between CML and Walt Disney Productions. The significance of this is that the case-law on which Mr Furness relies draws a distinction between royalties accruing to a settlement from licences or assignments of copyright effected by the settlor in his or her lifetime and royalties accruing from a disposal of copyright effected by the trustees themselves.

11. For HMRC Mr David Yates submits that the CML royalties derive from the 1994 agreement, made by PL Travers in her lifetime, giving them the character of income according to the case-law; moreover, they derive from the copyright in the Mary Poppins books, from which she received publication royalties from the outset, something which fortifies the conclusion that the royalties were income. Mr Yates contends that preserving them for the ultimate beneficiaries amounts to accumulating them; he adds that the division of the receipts between the legatees, the Cherry Tree Foundation and the trustees of the discretionary trust effected by the will does not amount to prudent provision against the wasting of the asset so as to escape being classified as an accumulation.

The law of copyright

12. It is convenient to preface our findings of fact with a brief summary of the English law of copyright, as restated with amendments in the Copyright, Designs and Patents Act 1988, about which there was no dispute. By sections 1(1) and 3(2), copyright is a property right which subsists in, among other things, original literary works once they have been 'recorded'. In the case of a literary work, copyright subsists until 70 years from the end of the year in which the author dies. By section 16, a copyright owner has the exclusive right to do certain things ('acts restricted by copyright'); these include copying, issuing copies to the public, performing in public and making an adaptation – in each case, either of the work or of a substantial part of it. Adaptation expressly includes (section 21(3)) making a version of a non-dramatic work (such as a Mary Poppins book) in which it is converted into a dramatic work (such as a stage show). Copying or performing an adaptation of a work is an act restricted by the copyright in the original work as well as by the copyright in the adaptation. Subject to limited statutory exceptions, the doing of any of these things by another person without the licence of the copyright owner is an actionable infringement.

13. The first owner of the copyright in a work is generally the author but, by section 90, copyright is transmissible by assignment or by testamentary disposition as personal or moveable property. Such an assignment or transmission of copyright may be partial, applying only to some acts restricted by the copyright and/or for only part of the period of the copyright. Copyright may also be licensed, either exclusively (in which case the copyright owner may not perform or license others to perform an act restricted by that part of the copyright that has been licensed) or otherwise. A licence of copyright is normally binding on successors in title of the copyright owner who grants it.

14. The law of copyright will be different overseas, though there is a measure of harmonisation of copyright laws under European Union law (including of the 70 year period of copyright) and possibly also pursuant to international conventions.

The facts

15. PL Travers published six children's books featuring Mary Poppins between 1934 and 1982. In 1960 she and a family company entered into an agreement with Walt Disney Productions under which they agreed to grant Walt Disney Productions an assignment of the right to make motion picture adaptations of any of the Mary Poppins books (subject to conditions as to approval of their content) and the sole and exclusive motion picture rights in the books, together with what would nowadays be called 'merchandising' rights. The rights assigned did not include dramatic, radio or television rights, but PL Travers undertook not to "exploit or otherwise deal with the dramatic, radio or television rights" in the books "except through and by arrangement with" Walt Disney Productions "upon such terms and conditions as may hereafter be mutually agreed". The assignment envisaged by this agreement was made, on similar terms, in 1962. In 1966 PL Travers set up the Cherry Tree Foundation charitable trust and settled upon its trustees the right to receive 9% of the receipts under the Disney agreement. Her right to receive payments from Disney was subsequently commuted for a lump sum payment, so that receipts from Walt Disney Productions are no longer in issue.

16. In May 1994 PL Travers made an agreement (which we have called the '1994 agreement') with David Pugh Ltd and CML with a view to a stage musical. This agreement warranted that PL Travers was the sole owner of the copyright in the Mary Poppins books but referred to the undertaking given to Walt Disney Productions. Clause 1 of the Agreement having provided for a non-refundable advance (which was paid), clause 2 licensed to David Pugh Ltd and CML, subject to the rights of Walt Disney Productions but for the life of the copyright in the books, "the entire complete and exclusive rights throughout the world and in all languages … to cause a dramatic-musical play to be written based upon" the books, to use the title *Mary Poppins*, and to present "the Show" (as it was called) as a First Class Production on the musical stage "anywhere in the Universe" and, conditionally on that having been done, to present the Show on the speaking stage anywhere in the Universe.

17. Clause 3 went on to provide that, if (a) the Show was launched in the West End of London within an option period expiring at the end of 1999 and (b) it ran for at least 21 days, there would be a "merger" of the rights in the Show "in and with the Show"; we take this to mean that PL Travers would cede to the producers any right of hers to restrain performances of the Show as being acts restricted by her copyright in the original books, but whether we are right in this does not matter. The more important thing is that clause 4 also provided, conditionally upon that merger taking place, for the exclusive licence under clause 2 to be replaced by an assignment of "all right title and interest of and in the nature of copyright in the Show belonging to PL Travers including the sole and exclusive right to exploit the Show and the Original Work [that is, material from the books] therein in any and all media throughout the Universe", including broadcasting. This assignment explicitly included film and video rights, Second Class stage rights (i.e. the right to authorise performances at venues other than first class venues such as are found in the West End and on Broadway), the right to exploit the Show in foreign translations or to adapt it, merchandising rights and various other rights. The agreement also contained provision as to royalties: for first class productions the royalty was the greater of 2% of takings or the product of a formula; there were formulae for calculating the royalty in respect of other exploitations.

18. Mr David Pugh and Sir Cameron Mackintosh thereafter attempted, unsuccessfully, to obtain approval from the Walt Disney organisation (which we shall refer to in future as 'Disney') for a stage musical to be put on by them; this approval was not forthcoming until 2004 (in circumstances we describe below). As a result, no stage show was put on in the London West End within the option period and consequently the merger and assignment provided for by clauses 3 and 4 did not take effect. The trustees were, however, forced later to accept – in our view realistically – that clause 2 had granted David Pugh Ltd and CML an exclusive copyright licence to write and stage a show (with Disney's consent), with the consequence that the trustees could not license or assign stage musical rights to anyone else. The drafting of the Agreement was unsatisfactory from PL Travers' point of view in that the licence in clause 2 (which was obviously necessary initially, since without it both the writing of the show and its performance would be infringements of her copyright) survived the expiry of the option period despite the preconditions of the merger and assignment clauses not having been fulfilled. We should explain that neither the trustees (who are current or former partners in Goodman Derrick LLP) nor anyone else in that firm had any involvement in the 1994 agreement, or even any knowledge of it, until after PL Travers' death.

19. PL Travers re-made her will in February 1996. We set out the parts of it relevant to this case at paragraph 53below. We note at this stage that clause 5(c) exempted the trustees from liability if they failed to maximise the receipts of the trust as a result of complying with the letter of wishes that accompanied the will. The letter of wishes said among other things that it was PL Travers' wish to have a stage drama or musical of Mary Poppins made from material in her books rather than in the Walt Disney film; she did not wish any stage play to be made that was based on the film.

(Anyone who has read any of the books and seen the film will be aware that the portrayal of Mary Poppins in the film is somewhat different from the character in the books. It is clear that PL Travers preferred her own creation to Walt Disney's.)

20. She died two months later. It was not until December 1999 that the trustees were told, in a letter from her literary agent, of an approach made to PL Travers by Mr David Pugh in 1993, of the subsequent involvement of Sir Cameron Mackintosh, of the 1994 agreement and of the unsuccessful negotiations conducted by Mr Pugh and, following his involvement, Sir Cameron Mackintosh with Disney. The letter went to say that Mr Pugh (who had in the meantime successfully produced the musical *Art*) had withdrawn from the project and assigned his company's rights under the 1994 agreement to CML.

21. The letter explained that negotiations with Disney had continued. It told the trustees that PL Travers had agreed during her lifetime that the option period in the 1994 agreement would be extended on terms which were to be agreed by the end of 1999; CML had made a proposal as to the terms. In addition Disney had themselves approached the literary agent, seeking to acquire the dramatic rights in Mary Poppins themselves and offering a substantial advance on royalties.

22. The trustees replied asking for a copy of the 1994 agreement, and had an initial meeting with the literary agent in January 2000. They took specialist legal advice on the effect of the agreement, wishing to contend that CML's rights had expired at the expiry of the option period (which had not been extended). Without disclosing the advice, one of the trustees, Mrs Diana Rawstron, accepted in her evidence to us that there were real difficulties in seeking rectification of the agreement to that effect.

23. Mr Furness did submit to us, though he realistically did not make it a major plank in his case, that the agreement was to be construed as containing an implied term to the effect that the rights granted by clause 2 expired if the preconditions for merger and assignment were not met. We do not accept that interpretation. We recognise that in a situation in which the preconditions for assignment are not met, the agreement leaves both parties in an unsatisfactory position: PL Travers and her successors in title could not license the writing of a show by anyone else even if CML never put one on at all; from CML's point of view, the attractiveness of investing in a show that was not launched in the option period would be reduced by the fact that CML would not receive an assignment of rights or obtain the valuable additional rights that we have summarised in paragraph 17. Nor would "merger" occur, with the consequence (it seems to us) that CML could not effectively license others to perform the show because the clause 2 rights did not include that right; PL Travers or her successor could therefore have prevented such performances as being an infringement of the copyright in the books. Mrs Rawstron made points of this sort in her evidence, clearly feeling (and we have some sympathy with this) that nobody who applied their mind to the drafting of the agreement could have intended to create the possibility for such a

situation. It appears that those handling the negotiations on PL Travers' behalf did not have the benefit of any legal advice.

24. Nevertheless, the law only implies terms that represent the common but unexpressed intention of the parties and do not contradict the express terms. The implied term contended for would contradict the express grant in clause 2 of a licence for the lifetime of the copyright, and there is no reason to believe that CML intended such a term to be implied. The agreement as written, though unsatisfactory, was from their point of view more favourable than one in which they risked losing everything the agreement gave them if (as indeed happened) protracted negotiations with Disney prevented them launching a show during the option period. (As we find below, non-fulfilment of the preconditions left CML in a contractual position that would probably not have enabled them to invest in a production but, as subsequent events show, the existence of the agreement helped CML bring the trustees to the negotiating table.) There have not been any proceedings for rectification.

25. The situation as the trustees discovered it to be in 2000 was that Disney remained keen to obtain the dramatic rights and would support the trustees in litigation against CML. Mrs Rawstron drew our attention to the letter of wishes and told us (and we accept) that before her death PL Travers had told Mrs Rawstron of her liking for Sir Cameron Mackintosh and her wish that he should produce a stage musical, though without mentioning the existence of the 1994 agreement. The trustees decided that they should meet Sir Cameron. It was apparent to them from the meeting that Sir Cameron too was keen to produce the musical and would not surrender his rights. The trustees then decided (in Mrs Rawstron's words) to join forces with him. Negotiations between Sir Cameron and Disney had broken down, so the trustees approached Disney with a view to exploring a way of realising PL Travers' wish for a stage musical to be produced by CML.

26. Following initial discussion between the trustees and Disney, four years of negotiations between the trustees, CML and Disney ensued. It is not necessary to set out the details. Early in 2002 CML and Disney reached agreement in principle on the allocation of artistic control and were moving towards agreement on choosing the writer of the 'book' of the show. The issue of the royalty rate of 2% under the 1994 agreement was raised later that year; CML would also be paying a royalty to Disney, some of whose material (from the film) was intended to be used in the new stage show, and negotiations were taking place over that as well as over the rate of royalty to be paid to the trustees.

27. The upshot was an agreement executed on 15 December 2004, amending the 1994 agreement. We were provided with a version of the 1994 agreement as so amended. The main relevant changes were as follows. References to the option period were deleted (save, no doubt accidentally, in one place where its retention does not change the sense); merger under clause 3 was no longer subject to any time limit for launching the production but required the prior approval of the trustees. The rate

of royalty for first class productions was reduced to 1½%, with special rates agreed for a small number of productions that were in contemplation. Merger gave rise to additional rights, over and above those provided for in 1994, in respect of exploitation in ice shows, theme park shows and musical revues; these rights were to be transferred to Disney. The royalty formula for second class productions and some other exploitations was amended. Rates of payment were introduced for the additional rights just referred to. Provision was made for certain approvals which under the original agreement would have been given by PL Travers to be given by Mrs Rawstron or a fellow trustee. Provision was also made allowing CML, following merger, to assign the benefit of the amended agreement to a joint venture company set up by it and Disney. CML paid the trustees an additional fee of £25,000 and a non-recoupable advance against royalties of £50,000. Mr Yates emphasised one respect in which the agreement was not amended: the grant of rights was still expressed to be by PL Travers. We observe that, while reference to David Pugh Ltd was removed and various references to the trust were introduced into the text, the agreement was still expressed to be between PL Travers and CML.

28. Sir Cameron Mackintosh's production of *Mary Poppins* opened in the West End on the day the amending agreement was executed, having had already been performed in Bristol. Subsequent events, so far as relevant, have been recorded at the beginning of this Decision.

29. Mr Furness's factual case on the events of 2000-2004 was that the CML royalties were in point of fact "derived from" the 2004 agreement and not the original 1994 agreement. The original 1994 agreement, he said, had never produced any royalties (though, as Mr Yates pointed out, it did produce a non-recoupable advance against royalties of £50,000). The evidence showed, Mr Furness maintained, that a renegotiation of the 1994 agreement was essential in order for a musical to be produced. One aspect of the amendments that was emphasised was the reduction of the first class royalty rate from 2% to 1½%, facilitating CML's ability to pay the level of royalty sought by Disney.

30. For the reasons we give later in this Decision we do not consider that the answer to the question raised by this case depends on whether the CML royalties are "derived" in a commercial sense from one or the other agreement; it is in our view a matter of analysing the legal effect of what was agreed in 1994 and 2004. But in case we are wrong about that, we record our finding that on the balance of probabilities the royalties whose tax treatment is in issue in these proceedings would not have been received by the trustees had they not intervened in 2000 in the then stalled negotiations between Sir Cameron Mackintosh and Disney. We also conclude on the balance of probabilities that no stage musical would have been produced between 1999 and now without some modification of the 1994 agreement. We have referred in paragraph 23above to the limited nature of the rights that CML could have insisted on. We do not think it probable that CML would have invested in the creation and production of a

stage musical, or that they could have offered to Disney terms sufficiently attractive to gain Disney's approval, on the basis solely of the rights given to CML by clause 2.

31. A further obstacle relied on by Mr Furness was doubt over whether CML had any rights, given the possibility of an argument that the agreement contained the implied term he contended for or was liable to be rectified. The trustees have obtained some after-the-event support for that argument from CML's lawyer. As to that, we have found the implied term to be barely arguable and Mrs Rawstron has acknowledged the difficulties of seeking rectification. This aspect of the issue has not contributed materially to the conclusion we have reached.

Case-law relevant to section 686, section 479 and their predecessor provisions

32. In *Carver v Duncan* [1983] STC 310, to which we were referred, Vinelott J saw no reason to give the word 'accumulated' in a predecessor provision to sections 686 and 479 a meaning different from that attributed to it in section 164 of the Law of Property Act 1925 and that section's statutory predecessors. We take the same approach. We have referred to *Howell v Trippier* in paragraphs 6 and 7above. It concerned complicated provisions in section 249 of ICTA 1988: trustees of a settlement, under which income was to be accumulated and the property of which included shares, had received bonus shares in lieu of a cash dividend. In consequence, section 249 charged tax on a deemed income, and the issue was whether the deemed income was itself deemed to be 'income which was to be accumulated' for the purposes of section 686. The Court of Appeal held that it was, as a matter of construction of section 249, despite the fact that the bonus shares themselves were treated by the settlement as capital.

33. Paragraphs 21 and 22 of the judgment suggest that, so far as the bonus shares themselves were concerned, their tax treatment was determined by the terms of the settlement. However, if a settlor can cause trust receipts to be treated as capital for the purposes of the tax provisions merely by virtue of directing the trustees to accumulate them, the sections would have no application; we consider that the Court of Appeal's acceptance that the terms of the trust treated the shares as capital must be predicated on the unstated premise that they did so legitimately since the shares represented either an increase in, or a realisation of, the value of the original shareholding. It seems to us to be implicit both in Vinelott J's approach and in *Howell v Trippier* that the word 'income' in the tax provisions must equally have the same (trust law) meaning as it bears for the purposes of section 164.

34. Section 164, which was repealed in 2010, formerly provided in part as follows:

164.— General restrictions on accumulation of income.

(1) No person may by any instrument or otherwise settle or dispose of any property in such manner that the income thereof shall, save as hereinafter

> mentioned, be wholly or partially accumulated for any longer period than one of the following, namely:—
>
> (a) the life of the grantor or settlor; or
>
> (b) a term of twenty-one years from the death of the grantor, settlor or testator; or [two further alternative periods that it is unnecessary to set out]
>
> In every case where any accumulation is directed otherwise than as aforesaid, the direction shall (save as hereinafter mentioned) be void; and the income of the property directed to be accumulated shall, so long as the same is directed to be accumulated contrary to this section, go to and be received by the person or persons who would have been entitled thereto if such accumulation had not been directed.

Subsection (2) went on to provide for certain exceptions.

35. Section 164 was the successor provision to section 1 of the Accumulations Act 1800, commonly referred to as the 'Thellusson Act' after the case of *Thellusson v Woodford* (1799) 4 Ves 227 in consequence of which it was enacted. In *Re Berkeley* [1968] Ch 744 at 780 Widgery LJ described its purpose as follows:

> In [*Thellusson v Woodford*], as is well known, a testator had directed an accumulation of the income of his estate during numerous lives in being at his death, with the result that distribution would be deferred for a very long period and a vast fortune created. The mischief at which the Act is aimed is a direction or power to accumulate income which is excessive in duration and unduly penalises the present generation of potential beneficiaries in order to amass capital for the benefit of a generation to come.

36. In the same case Harman LJ similarly described accumulation as involving "the addition of income to capital, thus increasing the estate in favour of those entitled to capital and against the interests of those entitled to income" (page 772).

37. We were taken to a number of authorities on the distinction between income and capital in trust law. They concerned settlements under which different beneficiaries were entitled to certain trust money depending on whether the money was capital or income. Typically there was a life tenant or income beneficiary, entitled to enjoy the trust property for a limited period (usually during that person's life) and/or to receive the income earned by the trust property during that period, and a 'remainderman' entitled to have the trust property passed to him at the end of the period. The cases shown to us included cases where the trust property included coal or iron deposits; in one case the principles derived from those cases were applied to copyright royalties.

38. It was a feature of the cases that the settlor had not specified whether the fruits of exploitation of the minerals or copyrights should be enjoyed by the life tenant or preserved for the remainderman. The issue in each case was whether the trust's receipts from the exploitation were to be paid to the life tenant or income beneficiary or to be preserved for the remainderman. It happened that all the cases on the classification of the receipts as capital or income in these circumstances were Scottish cases, though the first of them was a decision of the House of Lords in which the House pronounced that the position in English law was the same. We were shown the Report of the Law Commission on *Capital and Income in Trusts: Classification and Apportionment*, in which the Commission appears to treat some of those authorities as representing the position in English law also.

39. The cases hold, broadly, that the settlor may specify which beneficiary is to enjoy the receipts, but that in default of express provision the settlor will be taken to have intended that the life tenant should receive the receipts from mines that had already been worked or leased (or copyrights licensed or assigned) before the settlement came into being but that, where the trustees opened new mines or granted mining rights over additional mineral deposits or made fresh disposals of copyright, the trust's receipts from those sources were capital to be preserved for the remainderman.

40. The first of them is *Campbell v Wardlaw* (1883) 8 App Cas 641. There the testator had left his estate in trust and directed his trustees to pay to his widow "the whole annual product and rents" of the residue of his estate until her death or remarriage. The estate included some coal and iron mines in respect of which the settlor had granted mineral leases during his lifetime; in addition, the trustees granted some further mineral leases in respect of other mineral deposits that had not previously been let. They paid over to the widow the rents they received under the mineral leases granted by the settlor but refused to pay over the rents under the mineral leases they had granted after his death. The widow claimed those rents too, but the Court of Session's decision in favour of the trustees was upheld by the House of Lords.

41. Lord Blackburn LC put it as follows:

> "The principle upon which the whole matter depends is the same both in English and in Scotch law, and I should be inclined to think that it would be very much the same in every country, for it is the nature of things that causes it to be so. Where there is "produce," such as minerals, which, when once taken away, is never replaced, it is in a very different position from, I may say, apples or fruits of that kind, which are annually reaped and which replace themselves. That they are different in the nature of things is obvious enough. When there is an estate consisting partly of minerals or things of that sort, and partly of annual produce in the other sense, such as fruits and the like, and that estate comes to a person with a limited interest, the remainder being in somebody else, the question would arise, What is to be done with the produce? The law of England, and I believe of every country, the feudal law and the civil law too, would say that in that case

> the person who has the limited interest takes, beyond all doubt, the annual produce, the grass, the apples, and things of that sort, and applies them to his own use as he pleases, as long as his interest lasts. But it would follow, from the strict rule which I have mentioned before, that minerals, whether the mines had been opened or not, would remain a part of the soil belonging to the person who was to have the ultimate interest in the soil: the remainderman, as he would be called in England, or the fiar as he would be called in Scotland, would take them all.
>
> "But very early there was introduced this in favour of the person who takes a limited interest,—that where, at the time when the person having a limited interest comes into possession, minerals have been already opened, whether coal-pits or quarries, or the like, the person who has that limited interest shall be at liberty to continue to work those coal-pits or quarries which have already been opened....
>
> "I am inclined rather to agree ... that the original ground of all that was that there was supposed to be an irresistible indication of intention that he who conveyed the property for a limited time to a person with a limited interest intended him to work the opened minerals. I am inclined to think that it was upon that ground that the Courts originally acted throughout; and I quite agree with what Mr. Davey has said, that where there is a sufficient appearance of intention in the instrument to shew either that that should be restricted or that it should be extended, that intention would govern...."

42. The other speeches were to the same effect.

43. In *Cleland and others (Dick's Trustees) v Robertson* (1901) 3F 1021 the settlor had granted a mineral lease before his death but the tenant had never worked the mine and, two years after the settlor's death, took advantage of a break clause and surrendered the lease. Some years after that, another prospective tenant sought a lease of the same mine, which the trustees granted. The Court of Session held that, since the minerals in question had been made into 'profit-producing subjects' by the lease granted in the settlor's lifetime, the life tenants (or 'liferenters' as they are called in Scotland) were entitled to the rent received under the new lease. Mr Yates relied on this case in support of an argument that PL Travers had "opened the mine" at least when she granted rights to David Pugh Ltd and CML in 1994 – if not when she first published the books – and it was irrelevant that those companies had not worked it in her lifetime.

44. *Bow v Ranken* [1908] SC 3, upon which Mr Furness relied, is the only case to consider the Thellusson Act in the present context. The testator died in 1848, leaving his estate on trust to pay the income to certain relatives of his during their lifetimes and then to convey the estate to a remainderman. The estate included minerals that had never been worked and the will said nothing about them. In 1907 the trustees granted

a coalmining lease. Applying *Campbell v Wardlaw*, the Court of Session held that the rents and royalties received under the lease (both before and after the mineral tenant began working the mine) were capital on the ground (*per* Lord Low, with whom the other members of the Court concurred) that "the income to which the [income] beneficiaries are entitled ... does not include the produce of mines which were opened after his death". Turning to the Thellusson Act, his Lordship held

> "... the answer to the one question solves the other, because if we answer the third question [whether the receipts should be preserved for the remainderman] in the affirmative on the grounds that these rents are capital and not income, it follows that they cannot be struck at by the Thellusson Act, which refers to income only."

45. In *Naismith and others* (*Naismith's Trustees) v Naismith* [1909] SC 1380 the estate comprised some mines that had been let during the settlor's lifetime and another that was let by the trustees. The Court of Session held that the receipts from the new lease were to be preserved for the remainderman, regarding as "plainly unsound" the contention that "by letting minerals in other parts of the estate the [settlor] must be regarded as having opened up the minerals of his whole estate". The Court also held, following *Dick's Trustees v Robertson*, that future royalties in respect of a mine let during the settlor's lifetime but not yet worked would go to the life tenants on the ground that "the [settlor] having let the minerals, they are minerals which were opened in his lifetime, even although they were not worked".

46. In *Simpson and others (Davidson's Trustees) v Ogilvy* [1910] 1 SLT 45 the Court of Session applied these principles to copyright royalties. The testator, a Professor in Edinburgh, left a life interest in his estate to his niece, the remainder to the niece's children. He had published a number of books and articles on Hebrew language and theology during his lifetime, sometimes doing so in return for a lump sum payment and on other occasions in return for a royalty or share of profits. He also left some unpublished works, which his trustees published after his death, receiving a mixture of lump sums, royalties and profit shares. The Lord Justice-Clerk (with whom the other members of the court agreed) held that the receipts from works published in the testator's lifetime fell to be paid over to the niece, saying

> "I think the testator's intention is manifest. Of the books which he himself published he took the income for himself, and when he left the liferent of his estate to anybody, I think he must be held to have intended that that from which he was deriving income should be a source of income to the liferenter...."

He continued:

> "But I think it is a totally different case when you come to those works which were dealt with after the death of the testator. Whatever he left after his death, and had not dealt with during his lifetime – whether complete manuscripts or

incomplete manuscripts – were necessarily of the nature of estate left behind by him, which it was the duty of the trustees to realise to the best of their ability.... I am clearly of opinion that the works which passed into the hands of the trustees as part of the testator's estate, and which he had not dealt with except by leaving it to them, form part of the capital of the estate."

47. The receipts from those works were accordingly to be preserved for the niece's children. Lord Ardwall, concurring, referred to the mining cases.

48. Mr Yates was content that we should follow these decisions, reserving the right to contend on appeal that *Davidson's Trustees* did not represent the position in English law. We have, however, considered whether we are persuaded, or alternatively bound, by them. We are persuaded by them in the case of propositions relevant to the issues we have to decide and do not therefore need to investigate whether pronouncements of the House of Lords as to English law, made in a Scottish appeal, are binding on English courts and tribunals.

49. These authorities do not, however, resolve all the questions that we have to answer. The issue in them was simply which category of beneficiaries was entitled to receipts from mineral leases or copyrights in circumstances where the will was silent on the question. None of them were tax cases and, apart from *Bow v Ranken*, they did not deal with the application of s 164. We accept, on the authority of *Campbell v Wardlaw*, that it is open to a settlor expressly to provide for either category of beneficiary to be entitled: see Lord Blackburn's reference to "a sufficient appearance of intention in the instrument to shew either that [the presumption that the life tenant was to receive the proceeds of working already opened mines] should be restricted or that it should be extended". We take "restricting" the presumption to refer to allocating the proceeds of opened mines to the remainderman and "extending" it to refer to allocating the proceeds of new mines to the life tenant. Frustratingly for present purposes, Lord Blackburn does not offer an opinion on whether a settlor who does the former is thereby directing an accumulation of income within the meaning of what was then the Thellusson Act. Lord Blackburn must have known of the Thellusson Act but, since it does not prohibit such accumulations entirely, we cannot infer from his failure to mention it that he implicitly accepted that it was not engaged at all. Counsel's researches did not produce any other authority touching upon that question.

50. In accordance with Lord Blackburn's approach we have construed PL Travers' will and concluded that it does instruct her trustees as to whether the receipts from the Mary Poppins books are to be applied as capital or as income. We do not therefore need to consider further that aspect of the Scottish authorities that deals with the ascertainment of a presumed intention or to grapple for that purpose with the distinctions drawn between mines leased, surrendered and re-leased or between mines on one part of an estate being leased during the settlor's lifetime and mines on another part being leased by the trustees.

51. As far as s 164 is concerned we respectfully agree with the analysis (so far as it goes) in *Bow v Ranken*. It seems to us to be plainly right that, in circumstances where land containing untouched minerals is settled upon a life interest trust, the minerals form part of the trust property that is to be preserved for the remainderman. Where (as in some circumstances they may perfectly properly do) the trustees turn the minerals into cash, the remainderman's interest in the trust property would be eroded if the cash were applied as income and paid over to the life tenant since, as Lord Watson pointed out in *Campbell v Wardlaw* at page 649, "what we call a mineral lease is really ... a sale out and out of a portion of land". Preserving the proceeds of disposal for the remainderman is not within the mischief against which s 164 is aimed.

52. We consider that the same analysis applies to an assignment of copyright effected by trustees. Because of the way in which we have analysed the effect of the 1994 agreement as amended in 2004, we do not need to decide how s 164 applies to a licence of copyright effected by trustees or an assignment of copyright effected during a settlor's lifetime.

The construction of PL Travers' will

53. The relevant provisions of the will are detailed but we cannot avoid setting them out. They read as follows:

5 (a) I give all my Literary Estate as defined below to my Trustees

(b) In this Will "my Literary Estate" means all published and unpublished works of which I am the author and all manuscripts letters and other papers produced in the course of or otherwise relevant to or of interest in connection with my literary work together with all copyrights moral rights and other rights and privileges which may exist in any of the foregoing material

(c) I DIRECT that my Trustees shall give effect to the wishes which I have expressed to them regarding my Literary Estate and any exploitation of it and I DECLARE that my Trustees shall not be liable for any loss made in fulfilling those wishes

(d) Any payments received by my Trustees in respect of or [*sic*] any future commercial production or exploitation in any form whatsoever of any books I have written (including any sequel to the film "Mary Poppins") shall be held by my Trustees UPON TRUST to distribute in the following manner:

(i) to pay first out of the monies received by them and before making any other payments the sum of TWO THOUSAND FIVE

HUNDRED DOLLARS ($2,500.00) to each of [two named beneficiaries]

(ii) out of the remainder of such monies to pay 9% to the Cherry Tree Foundation ("the Foundation") or if at or at any time after my death the Foundation has ceased to exist or has amalgamated with another charity or has changed its name to such charitable organisations which they consider most nearly fulfils the objects of the Foundation and I direct that the receipt of a person who appears to be a proper officer of the charity receiving this gift shall be a full discharge to my Trustees

(iii) to hold the remainder of such monies as an addition to the residue of my estate

(e) Subject to (d) above any money received in respect of my Literary Estate shall be added to the residue of my estate

6. I GIVE all the residue of my estate (out of which shall be paid my funeral and testamentary expenses and my debts) and any property over which I have a general power of appointment to my Trustees ON TRUST to sell or retain it (and such estate and the property which currently represents it is referred to in this Will as "the Trust Fund")

7. My Trustees shall hold the Trust Fund upon the trusts set out in Clause 8 below

8. (a) In this clause

(i) "the Trust Period" means the period starting with my death and ending 80 years afterwards (and that period is the perpetuity period applicable to this clause)

(ii) "the Beneficiaries" means

(1) my son John Camillus Travers

(2) any issue of mine who are alive at the start of or born during the Trust Period

(3) the Cherry Tree Foundation

(b) My Trustees shall hold the Trust Fund and the income from it on such trusts in favour or for the benefit of all or any one or more of the Beneficiaries as my Trustees (being at least two in number or a trust corporation) in their absolute discretion may at any time or times during the Trust Period by any deed or deeds revocable or irrevocable appoint (regard being had to the rules about remoteness) and in making any such appointment they shall have powers as full as those of an absolute beneficial owner and in particular (but without prejudice to the generality of the foregoing words) may … [various powers were given to the Trustees by the remainder of this subparagraph and subparagraph (c)]

.....

(d) In default of and subject to any exercise of the powers given them by the preceding provisions:-

(i) during the Trust Period my Trustees shall pay or apply the income of the Trust Fund to or for the maintenance education support or otherwise for the benefit of such one or more of the Beneficiaries as my Trustees may in their absolute discretion think fit BUT with power (during the period of 21 years from my death) to accumulate such income or any part of parts of it (with power to apply the accumulations of past years as if they were income of the current year) AND with power (during the Trust Period) to resolve to hold the whole or any part or parts of such income as income on trust for any of the Beneficiaries absolutely and

(ii) on the expiry of the Trust Period my Trustees shall hold the Trust fund as to both capital and income ON TRUST absolutely for such of my issue as are then living and if more than one in equal shares per stirpes but so that no issue shall take whose parent is alive and so capable of taking

54. The trustees have not made any use of their powers under clause 8(b) or (c), so that the property of the settlement remains subject to the trusts of clause 5 and clause 8(d).

55. The parties are agreed that clauses 5 to 8 establish two separate trusts. The first, in clause 5, deals with PL Travers' literary estate, as defined: broadly, her manuscripts and papers in their physical form and her copyrights, including moral rights as protected by the 1988 Act, and any other rights in them. Clause 5 gives those things to the trustees. It is to be noted, though, that the trustees do not hold the literary estate on trust for any beneficiary or class of beneficiaries; the intention is not that any particular beneficiaries should own, in equity, the right to perform acts restricted by PL Travers' copyright or to license any others to do. Rather, payments received in respect of future production or exploitation of the Mary Poppins books are to be held on the trusts set out in clauses 5(d) and (e).

56. It was agreed that the word 'or' in the first line of clause 5(d) is superfluous; it was probably left in by mistake when a clause of a previous will was recast into the present clause. The obvious reading of the clause is one that ignores it. Clause 5(d) directs the trustees to deal in particular ways with payments received "in respect of

[...] any future commercial production or exploitation of" PL Travers' books: first, and before applying the money in any other way, to pay $2,500 each to the two individuals named in clause 5(d)(i); once that duty has been discharged (as by now it has been), further receipts are to be divided into fixed shares: 9% to be paid to the trustees of the Cherry Tree Foundation and the remainder to be held by the trustees "as an addition to the residue of my estate".

57. Clause 5(e) then directs that any other money received in respect of PL Travers' literary estate should be added (in whole) to the residuary estate. It is not entirely clear to us what money might be "received in respect of [the] literary estate" within the meaning of clause 5(e) whilst falling outside the definition in clause 5(d), which takes precedence over clause 5(e). The issue is not relevant to our decision; it is common ground that the payments received by the trustees from CML fell within clause 5(d), and money which comes into the residue by virtue of either clause receives the same subsequent treatment.

58. Clause 6 then gives all the residue of the estate (after legacies, debts and expenses) to the trustees and renames it 'the Trust Fund'. By that stage the residue includes money added to it under clauses 5(d) or (e). Clause 7 then introduces clause 8, which sets out the further trusts. The very wide powers to vary the trusts given to the trustees in clauses 8(b) and (c) not having been used, it is unnecessary to consider them. The trust applying in default of exercise of those powers, by virtue of clause 8(d), requires the trustees to distinguish between income and capital: under clause 8(d)(i), which applies during the trust period of 80 years from PL Travers' death, they may only deal with income, either applying it for the benefit of any of the beneficiaries, accumulating it for a period permitted under s 164 (which was still in force when the will was drafted) or resolving to hold particular parts of it for a particular beneficiary exclusively. After 80 years they are to hold the capital and income in fixed shares – in such a way that (putting it incompletely) the members of the most senior generation of PL Travers' issue with a member then living will receive equal shares, with the issue of any deceased member of that generation having what would have been their deceased parent's share divided equally between them.

59. The income dealt with by clause 8(d)(i) is "income of the Trust Fund". The question therefore arises whether that "income" includes receipts such as the CML royalties. We have concluded that it does not. The obvious meaning of the expression "income of the Trust Fund" is income earned by the Trust Fund – deposit interest, investment dividends and the like. The stream of receipts represented by, for example, the CML royalties is not income earned by the Trust Fund; it is, rather, a stream of accretions to the Trust Fund which find their way into it *via* clause 5(d) or 5(e) and then clause 6. Accordingly we conclude that the trustees are directed by the will to preserve the CML royalties for those who will satisfy the conditions of clause 8(d)(ii) in 2076. In this respect the settlement is similar to the Scottish cases that we have discussed. Mr Yates disputed that the settlement directed the trustees to treat the royalties as capital on the ground that clause 5 merely required them to add the

royalties to residue. He agreed, however, that adding them to residue resulted in their being dealt with in the manner in which residue was directed to be dealt with. We consider that when both the clause 5 trust and the clause 8(d) trust (as we have construed it) are taken into account, there is a direction to treat the royalties as capital.

Are the CML royalties 'income' for the purposes of the law of trusts?

60. The next issue is whether, in directing her trustees to preserve the CML royalties for the beneficiaries identified in clause 8(d)(ii), PL Travers has directed an accumulation of 'income' within the meaning of s 164 of the Law of Property Act so as to bring into play sections 686 or 479 and 480 of the successive tax statutes.

61. Mr Furness submitted that this was not such an accumulation of income, submitting that the CML royalties were not 'income' in the trust law sense and/or that they were not being 'accumulated' in the trust law sense because they were being stored up to replace the wasting asset represented by copyrights that will expire (under current legislation) in 2066.

62. Mr Furness submitted that the CML royalties were the fruits of the 2004 agreement or alternatively that the cases permit a testator to choose to designate receipts from mining or exploitation of copyright as capital. We agree with that second submission to the extent that those cases, which were confined to deciding the question of which category of beneficiaries was entitled to the receipts and (apart from *Bow v Ranken*) did not discuss the Thellusson Act, leave the settlor free to direct how the receipts should be applied; but a settlor cannot, by her choice of words, dictate how her trust should be taxed nor whether it escapes the constraints formerly imposed by s 164. Rather, the fiscal provisions (and, formerly, s 164) must apply or not depending on whether or not those provisions recognise the receipts as amounting to income and the manner in which they are directed to be applied as amounting to accumulation. This part of Mr Furness's argument seemed to take it for granted that the consequence of a settlor directing that such receipts be preserved for the remainderman was that s 164 treated them as having had a capital nature all along. We do not consider that that consequence necessarily follows.

63. In addition to his argument based on the terms of the will, Mr Furness submitted that the CML receipts were not income for essentially two self-standing reasons: one was that they derived from the 2004 agreement, so that the principle in *Bow v Ranken* applied. The second (if the first was not accepted) was that they were in any event the proceeds of sale of what the Copyright Act explicitly designates as property; he compared a case in which a testator had sold a piece of land for a price payable in instalments and died before all the instalments had been paid. The instalments, he submitted, were capital which replaced the former tangible capital asset, whether they were paid before or after the testator's death. He also pointed to the additional rights that the 2004 agreement gave to CML.

64. In response Mr Yates submitted, in reliance on the mining lease cases, that the CML royalties were income. He pointed out, accurately, that PL Travers' rights of copyright that underpinned the 1994 and 2004 agreements were her rights in respect of the Mary Poppins books. As he put it, the analogy in this case to the mines in those cases was Mary Poppins. That mine, he submitted had been opened in PL Travers' lifetime: she had derived royalties from Walt Disney Productions as long ago as the 1960s, as well as a payment on account of royalties from David Pugh Ltd and CML in 1994, and had derived royalties from the sale of the books since the 1930s. The present case was, he submitted, analogous to *Dick's Trustees*, which we have summarised in paragraph 43above – indeed *a fortiori*, since there had been commercial exploitation in her lifetime of the rights she and granted.

65. We have concluded that Mr Furness's case largely succeeds. We begin our analysis with the royalties (or, in the case of the 'additional rights' granted for the benefit of Disney, payments) in respect of the additional forms of exploitation, over and above those permitted by clause 2 of the 1994 agreement, that have been received as a result of the 2004 agreement.

66. At the time of PL Travers' death, clause 2 of the 1994 agreement had given CML and David Pugh Ltd a licence of certain of the stage show musical rights arising out of the Mary Poppins copyright, and clauses 3 and 4 had given them the contingent right to an assignment of those and further rights. Since the contingency had not been satisfied at the time of her death, the position at that time was that the rights covered by clauses 3 and 4 remained with her and that portion of her copyright passed into her estate. On 31 December 1999 the condition precedent to CML's right to an assignment became incapable of satisfaction, removing the possibility that those rights would leave her estate other than by the volition of the trustees.

67. The subsequent execution by the trustees of the 2004 agreement did not alter the clause 2 licence save as to the rate of royalty, but the retrospective deletion of the option period revived CML's contingent right to an assignment. The condition precedent to an assignment, namely 'merger', became once again capable of satisfaction. We were not told in evidence whether the merger and assignment have subsequently occurred but, given their favourable consequences for CML and Disney and their propensity to generate additional royalties, we would be surprised if they had not. In short, the trustees' execution of the 2004 agreement brought about the assignment to CML of the right to perform or licence others to perform, further acts restricted by PL Travers' copyright over and above those covered by clause 2.

68. The case is in this respect analogous to *Davidson's Trustees*, in that PL Travers' trustees have, in pursuance of their duty to maximise the value of the trust property in a manner consistent with PL Travers' wishes, themselves disposed of portions of her copyright that had come to the trustees at her death. It is also analogous to *Bow v Ranken*: because these portions of copyright had come into the trust, they were (intangible) property of the trust that fell in principle to be preserved for the clause

8(d)(ii) beneficiaries (though their preservation in an unaltered state would have been of little value to them insofar at least as the copyright subsisted under the law of European Union countries, since on the present state of the law they would have expired ten years before the beneficiaries' interests vested). Moreover, what the trustees did resulted in an assignment of the relevant portions of copyright, with the result that they no longer belonged to the trustees but were replaced by a stream of receipts that Mr Furness was in our view correct to analyse as proceeds of disposal of property by the trustees, retaining as a result their capital nature in the eyes of the law of trusts. This preservation for the clause 8(d)(ii) beneficiaries of the proceeds of replacing trust property by cash is therefore not an accumulation of what the law of trusts regards as 'income'. We do not need to decide whether the position would have been different if the trustees had instead granted a licence.

69. This conclusion resolves the position as regards CML royalties generated from forms of exploitation not permitted by clause 2. As regards the forms of exploitation covered by clause 2, the position in our view differs in the periods before and after the assignment.

70. We start from the proposition that the licence, albeit permanent and exclusive, that PL Travers had granted in her lifetime is not the same as an assignment; it leaves the ownership of the copyright with the licensor, creating a relationship between licensor and licensee analogous in some respects to that of a freeholder and leaseholder of land. The portion of PL Travers' copyright represented by the right to restrict the forms of exploitation described in clause 2 therefore passed into PL Travers' estate but (because the licence was binding on the trustees as her successors in title) did so burdened by CML's clause 2 rights. As regards the forms of exploitation covered by clause 2, the actions of the trustees in 2004 merely transferred to CML the ownership of the right to do things that it already had permission to do.

71. We have concluded that royalties received *after* that assignment in respect of forms of exploitation previously covered by clause 2 are nevertheless not income of the trust. This is because the effect of the assignment was that that portion of the copyright ceased to be trust property with effect from the date of the assignment. An analogy would be a settlement of real property which included the reversion of a lease. If the settlor directed the trustees to accumulate the rental income for the remainderman, he would be directing an accumulation of income. But if the trustees sold the reversion, they could legitimately preserve the proceeds of sale (though not the income generated by investment of them) for the remainderman. They could do so whether those proceeds were paid in a single sum or in instalments. Returning to the metaphysical world of intangible property, that seems to us to be what the trustees have done here. The fact that the proceeds of sale are a stream of payments triggered by the same events as under clause 2 does not seem to us to affect the analysis. For these reasons we do not consider that any CML royalties generated after the assignment are income of the trust within the meaning of s 164.

72. The position in respect of royalties generated *prior* to the assignment is different if we are right in the analysis of the position between PL Travers' death and the assignment that we have set out in paragraph 70. We have concluded that the portion of copyright represented by the right to restrict forms of exploitation covered by clause 2 did pass into the trust, on the ground that PL Travers did still own that portion of copyright at her death. The exclusive licence precluded her using that property in any way other than receiving royalties pursuant to the 1994 agreement but, had she received any, she would have done so in her capacity as copyright owner.

73. We do not consider that the fact that clause 8 of the will directs the trustees to preserve all the CML royalties for the clause 8(d)(ii) beneficiaries of itself produces the consequence that royalties paid under clause 2 of the 1994 agreement prior to the assignment are not income for trust law purposes. On our analysis, they are a stream of payments generated by property (the relevant portions of copyright) settled on and, in the period prior to the assignment, remaining with the trustees; that, we consider, is sufficient to characterise them as income. If an analogy with the Scottish cases is relevant, the royalties are a stream of payments the potential for which was opened up by PL Travers in her lifetime.

74. There are two competing analyses of a situation where a settlor settles land whose minerals have been leased or copyrights that have been licensed. Mr Furness's preferred analysis is that payments under the lease or licence are proceeds of sale of the tangible or intangible property involved which, from the point of view of s 164, can legitimately be preserved for the capital beneficiary. As to that, we accept that a remainderman is entitled to have preserved for him that which entered the settlement at the outset or the proceeds of its subsequent disposal. But in the situation under discussion the minerals or copyrights have passed into the trust already burdened by the lease or licence. The settlor has in his lifetime put it out of his power to restrain the use of the mine or copyright in accordance with the lease or licence, exchanging that power for a stream of monetary payments. The remainderman accordingly has no expectation that the minerals will remain in the ground or that the already licensed portion of copyright will be capable of exploitation by the trustees for his benefit inconsistently with the licence. To preserve for the remainderman the financial proceeds of the transaction with which the minerals or copyright were already burdened when they fell into the trust amounts, we consider, to undoing what the settlor has done in his lifetime by way of turning them into a stream of payments having the character of income.

75. We do not consider that the fact that the receipt of royalties in this case was dependent on agreement being reached with Disney affects the analysis; nor does the fact that no agreement was reached in time to enable a stage musical to be launched within the option period. None of those matters could affect the character of any royalties that were received. Similarly, our finding that, as matters stood by 2000, no royalties would in practice have been earned under clause 2 without the intervention of the trustees does not in our view change the analysis. Neither the fact that, because of

Disney's pre-existing rights, the generation of any royalties was uncertain nor the fact that the trustees' intervention was effective to break the deadlock can alter the fact that royalties under clause 2 were a stream of payments generated by property that was (prior to the assignment) in the trustees' hands but burdened by the transaction that PL Travers had entered into in her lifetime. If necessary, we find that concluding the 2004 agreement was analogous to re-leasing a formerly leased mine (*cf Dick's Trustees*).

To the extent that the CML royalties were income, were they being accumulated?

76. If we are right in what we have decided so far, this issue is only relevant to royalties received pursuant to clause 2 of the 1994 agreement prior to the assignment. This part of Mr Furness's case relied upon some authorities on s 164 of the Law of Property Act (and, before it, the Thellusson Act). We accept that, if the direction to the trustees in clauses 5 and 8 of PL Travers' will would not have brought about an accumulation restricted by s 164, then it will not engage sections 686 or 479 either. We do not, however, accept his submission that the direction escapes being a direction to accumulate.

77. The authorities on which he relied (none of which concern intangible property) establish that there is not an accumulation where income is applied to maintain an asset, or provide a substitute for the value of a wasting asset. We accept that copyright is a wasting asset in the same way as a leasehold interest or other time-limited form of property right.

78. The authority most directly in point is *Re Gardiner* [1901] 1 Ch 697, where the settlor owned some leasehold houses which were in turn subleased to tenants. He directed his trustees to collect the rents and, after applying them to pay the rents payable to his lessor and other outgoings, "to set apart ... the clear yearly sum of £50, which said sum of £50 I direct my trustees to pay and apply in or towards the effecting and keeping on foot a policy or policies in some good insurance office in London to secure the replacement at the termination of the said term of the capital that will be lost through not selling the said leaseholds". Buckley J held

> "What the testator has here directed is not, in my opinion, an accumulation within the Act. All that he has done is to direct that the property shall not be diminished. At the end of the term the leaseholds will be gone, and his scheme is that the money shall be there to replace them. Therefore, on principle, I do not think that this is an accumulation.
>
> "... the trustees here do not pay premiums so as to get an increase: they simply put them together in a heap so as to have the same and not an increased property at the end of the term."

79. The judgment does not explain the basis of the conclusion that the value of the insurance policies would be commensurate with the previous value of the leaseholds,

but was clearly predicated on that being the case. The judge also referred to *Re Mason* [1891] 3 Ch 467, to which we were also taken, describing it as authority

> "... to the effect that a trust to apply rents in repairing and reinstating buildings is not within the Thellusson Act. Repairing is putting property into as good a state of repair as it formerly was. In *Vine v Raleigh* [1891] 2 Ch 13 the Appeal Court drew a distinction between repairing old houses and putting up new houses and held that repairs were outside the Act.... [A]n improvement which adds to the property is within the Act, but an improvement which only keeps up the property is outside the Act. The decision in *Re Mason* is to the same effect. Stirling J there held that a trust for applying rents and profits in payment of ground rents and keeping buildings insured against fire and in tenantable repair and investing the surplus was valid so far as it was a bonâ fide provision for the performance of the trusts for rebuilding, repairing and reinstating the buildings. Applying the principle of these cases to the present case, it appears to me that this so-called accumulation being one which simply keeps up the property to its present value is valid and is not within the Thellusson Act."

80. Mr Yates showed us *Re Rochford* [1965] 1 Ch 111, in which a settlor had directed that estate duty that became payable under the then legislation upon the deaths of beneficiaries should be paid out of income. Holding that this was caught by s 164, Cross J described *Re Mason*, *Vine v Raleigh* and *Re Gardiner* as cases which

> "... undoubtedly show that a provision for accumulating income which goes no further than a prudent owner would go in the management of the property in question is not within the Act. A prudent owner of a wasting asset such as a lease sets aside some part of the rent to form a sinking fund, and a prudent owner of house property sets aside some part of the rents to meet future liabilities for repairs and rebuilding. No doubt a prudent owner of any form of property has in mind the impact of estate duty on his death.... [I]t may be that, by analogy to the cases referred to the courts ought to treat a provision for applying a reasonable proportion of the income of settled property in recouping capital for the amount paid in duty ... as not within the Act at all. But I do not think one can fairly deduce from these cases that any provision for accumulation, even if it extends to the whole income, is outside the Act if it simply directed to making good capital losses."

81. Mr Furness submitted that the direction to preserve 91% of the royalties (which is the combined effect of clauses 5(d) and 8(d)) made reasonable provision for the wasting of the intangible assets. Mr Davey retorted that the percentage was arbitrary and unrelated to the value of the copyrights. Our conclusion is that the wasting nature of the copyrights does not save the terms of the will from being a direction to accumulate, for the following reasons.

82. We accept that s 164 would not, in principle, preclude PL Travers from setting up a fund, funded out of income, to replace the value of the copyrights upon their expiry in 2066, in a manner analogous to *Re Gardiner*. The copyrights will have had a monetary value, which in principle will have been highest when they first passed into the trust at her death, and at that point had the longest period remaining to run. In principle the value will have been the amount that a willing buyer would be prepared to pay in return for an assignment of the copyrights (insofar as not disposed of during her lifetime) and the concomitant right to exploit them and receive the fruits of exploitation. That monetary value may well be difficult to gauge – we do not know to what extent there exists a market in literary estates – but it would in principle be the net present value of the predicted stream of receipts from exploitation over the ensuing 70 years.

83. We can see no reason, however, why that market value should be equivalent to 91% of the aggregate amount received in receipts from exploitation by the end of the 70 year period. On the contrary, it would almost certainly be less. We accept that the fund of accumulated receipts will not include income generated from investment of the receipts, which (at least after 21 years) will be distributed to the clause 8(d)(i) beneficiaries, but it would nevertheless fall to be discounted to arrive at the net present value of the stream of predicted receipts as at 1996.

84. In so concluding we are not convicting PL Travers of any lack of bona fides. On the information available to us we see no indication that she was attempting to emulate the testator in *Re Gardiner* at all. The Cherry Tree Foundation's 9% share of royalties reflects the proportion of the Disney royalties that she had originally settled on the Foundation in 1966.

Conclusion

85. For the above reasons we allow the appeal in part. We decide (a) that payments received by PL Travers' trustees pursuant to clause 2 of the 1994 agreement (as amended) in respect of the period prior to the merger and assignment of rights pursuant to clauses 3 and 4 of the agreement are taxable at the rate applicable to trusts by virtue of s 686 of ICTA 1988 (or, in the unlikely event that the merger and assignment had not occurred prior to the change in legislation, at the trust rate by virtue of s 479 of the Income Tax Act 2007) but (b) that payments received by the trustees in respect of the period following the merger and assignment of rights are not so taxable.

86. 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.

NICHOLAS PAINES QC
TRIBUNAL JUDGE

JILL GORT
TRIBUNAL JUDGE

RELEASE DATE: 14 August 2013