Neutral Citation Number: [2011] EWHC 3391 (Ch)

Case No: HC-11-C02437

**IN THE HIGH COURT OF JUSTICE**
**CHANCERY DIVISION**

Royal Courts of Justice
Strand, London, WC2A 2LL

Date: 15/12/2011

**Before :**

**MR JUSTICE BEAN**

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**Between :**

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| **DALRIADA TRUSTEES LIMITED** | **Claimant** |
| **- and -** | |
| **(1) DAVID ALEXANDER FAULDS**<br>**(2) ATHENA PENSION SERVICES LIMITED**<br>**(3) MINERVA PENSION SERVICES LIMITED** | **Defendants** |

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**Andrew Spink QC and Fenner Moeran** (instructed by **McGrigors LLP**) for the **Claimant**
**Nicolas Stallworthy QC** (instructed by **Gateley Manchester LLP**) for the **First Defendant**
**James Clifford** (instructed by **Freedman Law**) for the **Second and Third Defendants**

Hearing dates: 29 November 2011 - 1 December 2011

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# Approved Judgment

I direct that pursuant to CPR PD 39A para 6.1 no official shorthand note shall be taken of this Judgment and that copies of this version as handed down may be treated as authentic.

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MR JUSTICE BEAN

**Mr Justice Bean :**

1. This case concerns six Revenue registered occupational pension schemes ("the Schemes"), with a total membership of at least 487 members and funds of originally approximately £25 million.

2. The Schemes operated something called a 'Pensions Reciprocation Plan' ("PRP"). The PRP was conceived as a way of getting members access to their pension capital prior to retirement but without breaching HMRC rules. At the heart of the PRP model was a structure called a "Maximising Pension Value Arrangement" or "MPVA", whereby:

    i) Scheme Y would 'loan' funds to a member of Scheme Z, and reciprocally

    ii) Scheme Z would 'loan' the same amount of funds to a member of Scheme Y.

3. The principal question raised by the current proceedings is whether those MPVA 'loans' were made pursuant to valid exercises of the Schemes' respective powers of investment or whether they were invalidly made and thus void. At this trial I have been asked to consider:

    i) the question of validity;

    ii) a question that the Defendants have raised concerning the validity of two recent purported amendments, the first to each of the Schemes' power of investment and the second to each of the Schemes' power to meet expenses, in the case of the former of which it appears they consider may have had the effect of "curing" any prior invalidity there may have been in relation to the MPVAs (question 7A on the Amended Claim Form); and

    iii) a question raising an issue of estoppel as well as other subsidiary issues following on from the MPVA validity question (question 8 on the Amended Claim Form ).

*The parties*

4. The Claimant is a professional trustee company. On 31st May 2011 it was appointed as a trustee over thirteen pension schemes, generally described as the "Ark Pension Schemes", which included the six Schemes the subject matter of this litigation. Its appointment was made by the Pensions Regulator pursuant to s 7 of the Pensions Act 1995 ("PA 1995"). The Claimant's appointment arose out of the Pension Regulator's concern over the PRP business model. Although the appointment did not remove the existing trustees, under the appointment the Claimant is entitled to exercise all the powers of the trustees to the exclusion of the other trustees (PA 1995 s 8(4)) - effectively it therefore acts as a sole trustee in this matter.

5. As one of the trustees of the schemes (and as the only one not to have had involvement in the events giving rise to these proceedings), the Claimant is seeking to

represent all members and those claiming through them in whose interests it is to argue that the MPVA loans were not, and would not be in future, valid.

6. The First Defendant is a member of the Woodcroft House Pension Scheme. A representation order is sought for him to represent all members, and those claiming through them, in whose interests it is to argue that the MPVA loans were, and would in future be, valid. Although he has transferred his pension funds into the scheme, he has not received an MPVA, as before this could occur the Claimant was appointed as one of the Trustees. However, it may well still be in his interest to argue that the MPVA loans were valid, as this would be the only way he could obtain an MPVA loan in the future, and Mr Nicolas Stallworthy QC on his behalf argued in favour of the MPVA loans having been validly made.

7. The Second and Third Defendants are the original trustees of the Schemes when they were each established ("the Original Trustees") and were the only trustees prior to the appointment of the Claimant as one of the Trustees. The Original Trustees were the trustees who made the MPVA loans. Mr James Clifford, on their behalf, supported the argument (principally advanced by the First Defendant) that the MPVA loans were valid, and himself advanced the argument that the purported amendments recently introduced by the Schemes' sponsoring "employers" are valid.

8. I observe that although pension schemes of the type under consideration are classified as "occupational pension schemes" and the principal sponsor is traditionally referred to as the "employer", those terms have in cases such as the present one no more than a vestigial meaning. It is sufficient to qualify a scheme for registration if it has a single employee; others, not employed by the sponsor, can then join in large numbers. The investors here were not employed by any of the sponsoring companies.

9. The correspondence indicates that HMRC has been invited to join in the proceedings and/or to agree to be bound by the decision, but has declined both options.

*The Pensions Reciprocation Plan*

10. The PRP was conceived as a way of getting members access to their pension capital prior to retirement but without breaching HMRC rules. It operates as follows:

    i) An individual (Member A) with a pension "pot" in another, unrelated pension scheme is introduced to one of the Schemes (Scheme Y).

    ii) Member A obtains a transfer of his benefits from his original pension scheme to Scheme Y.

    iii) A 5% "standard fee" from the transfer sum is paid to the promoters of the PRP, and the remaining 95% of Member A's transfer value is used as follows:

        a) Up to 50% of Member A's funds in Scheme Y is 'lent' to a member (Member B) of one of the other Schemes (Scheme Z) under an MPVA 'loan'.

        b) A reciprocal MPVA 'loan' of equal value is then made by Scheme Z to Member A, using Member B's funds.

c) The remaining funds of both schemes are then invested in other assets.

11. The evidence of Craig Tweedley for the Defendants makes it clear that the purpose of the PRP Model was to set up a scheme which would "enable pension scheme members to have early access to a payment" from their pension fund in a way that complied with HMRC rules.

12. Mr Tweedley's witness statement goes on to say that the decision to allow a member to take an MPVA was one in which he was not involved. It was a matter for Athena and Minerva as trustees of the schemes. He expresses the belief that not all potential members' applications were accepted, but Mr Spink QC for the Claimant submits that there is no evidence from the trustees indicating whether any application was in fact rejected, and if so why.

13. According to Mr Tweedley the retirement "pot" available to a member who had taken an MPVA would comprise, on the vesting of his pension, the return made on the part of his fund invested by the trustees of his scheme in what might be described as orthodox investments, specifically property; and the right to be repaid the MPVA Discharge Amount (the sum originally loaned plus 3% simple interest per year, rolled up) owed by a member of a reciprocal scheme. But although the illustrative literature issued by the promoters of the PRP gave examples of directly paired members (Member A in Scheme Y and Member B in Scheme Z as set out above), the schemes were non-sectionalised: clause 1.2 of each Scheme's Trust Deed states that "no person has any right to any particular assets of the Scheme". This did mean that in the event of the death of or default by Member B of Scheme Z in the above example it would be the MPVA lenders in Scheme Y generally who would bear the loss, rather than it all falling on Member A. An exact pairing or matching rule, apart from concentrating the risk, would also have depended on the two MPVA loans being repayable at the same time, and on neither borrowing member having sought to transfer his fund to another pension scheme.

14. Another ground on which Mr Spink criticises the PRP Scheme is that its financial modelling assumed an average rate of return on the non-MPVA investments of between 8% and 9% over a 25 year period for a sufficient sum to be generated to discharge the MPVA obligation. It is right to say that the modelling for a 10 year loan, where only 25% of the fund would be the subject of the MPVA, assumed only 5% average growth. But the 25 year period was apparently (and understandably) the most popular, and a predicted rate of return in excess of 8% does seem unduly optimistic.

15. The promoters of the PRP who received the 5% fees referred to above were three connected limited liability partnerships: Ark Business Consulting LLP, Ark Commercial Pension Planning LLP and Ark Commercial Retirement Planning LLP. These were connected not only to each other but to Athena Pension Services Ltd and Minerva Pension Services Ltd, who were the Original Trustees and are the second and third defendants in these proceedings. Craig Tweedley is the sole shareholder in Athena and Minerva. Andrew Hields is the sole director of Athena and Carl Hanson the sole director of Minerva. Mr Tweedley, together with his wife and children, indirectly own Ark CPP and Ark CRP; and members of the Tweedley family together with Mr Hields and Mr Hanson own Ark BC. Mr Tweedley's daughter Rebecca is a director of four of the six sponsoring "employers".

*The Schemes' Deeds and Rules*

16. It is convenient to take the Trust Deed and Rules of the Lancaster Pension Scheme as representative of all six Schemes operating the PRP.

17. Clause 1 reiterates that the Scheme is established under irrevocable trusts (clauses 1.1 & 1.2); and by clause 1.5 provides:

> "Any provision of the Scheme (including any power, right, duty or discretion and any benefit and the terms on which it is paid) shall be read and administered as if there is an overriding requirement that it is subject to the same being consistent with Scheme Status and subject to compliance with any applicable statutory or regulatory provisions and also to any requirements of the Pensions Authorities. Nothing in the Scheme entitles any person to an Unauthorised Payment."

18. Clause 4.1 provides:

> "The Trustees and any Administrator have and may exercise all powers rights and discretions necessary or appropriate to enable them to carry out the purposes of the Scheme. Without restricting this they shall have the powers rights and discretions given to them by law and the specific powers rights and discretions set out in the remainder of this Clause so long as they are consistent with the law. If a law is framed so as to allow something the Scheme shall be deemed to include such a power and the ability to exercise it to its full extent."

19. Clause 6 provides at clauses 6.3-6.4:

> "6.3 A Trustee may do things and take decisions in relation to the Scheme even if the Trustee has a personal interest.
>
> 6.4 The protections in this Clause apply to former trustees. They also apply to directors of a company that is acting as a Trustee but subject to any restrictions that the law imposes".

20. Clause 8 provides:

> "8.1 The Trustees shall, subject to complying with any statutory restrictions on the investment of pension scheme assets, have power to invest, apply or transact with the whole or part of the Fund in their absolute discretion and as though they were beneficially entitled. Without restricting that general power, the investments may be of any kind anywhere in the world, whether tangible or intangible and whether or not producing income, and whether alone or together with others, and the investments may include any contracts or policies of investment or insurance, collective investment schemes, mutual funds, annuity contracts or managed fund arrangements.

> 8.2 The Trustees may select and notify Members of any Investment Facilities. The Trustees may add to, vary or withdraw any Investment Facilities".

21. Clause 10 provides:

> "Any costs, liabilities and expenses properly incurred by the Trustees in connection with the Scheme shall be met out of the Fund. The Trustees may decide that specific cost arrangements should apply to any transaction that applies to a Member's Account."

22. Clause 11 provides:

> "The trusts of the Scheme and the Rules may at any time be amended in writing by the Principal Sponsor. Any amendment must comply with any applicable statutory requirements. If a notice is given in a format agreed by the Principal Sponsor and the Trustees the Scheme shall pending the execution of any deed or other document be deemed to be amended in such manner as is necessary to give effect to the contents of the notice."

23. Clause 16 provides:

> "Appendix 1 of the Rules shall in respect of any benefits to which it applies override any other provision of the Scheme where there is any inconsistency. The Trustees may restrict any benefit or option a Member has under the Scheme accordingly."

24. The overriding Appendix 1 (to which clause 16 refers) provides:

> "This Appendix 1 does not confer on or provides any entitlement to rights or benefits under the Scheme in addition to those set out in the Rules.
>
> None of the benefits under the Rules shall be paid or administered in such a way as to breach any of the provisions of this Appendix 1 or otherwise prejudice Scheme Status. ...
>
> The terms used in this Appendix 1 have the meanings given to them under the [Finance Act 2004].
>
> A. AUTHORISED MEMBER PAYMENTS
>
> Benefit Rules
>
> Notwithstanding anything to the contrary in the Scheme, and subject to any transitional provisions in Part E of this Appendix 1, the payment of any benefits permitted by the Rules of the Scheme shall comply with;

> 1.1 The Pension Rules
> 1.2 The Lump Sum Rules
> 1.3 The Pension Death Benefit Rules
> 1.4 The Lump Sum Death Benefit Rules
> 1.5 The Recognised Transfer Rules
> 1.6 The Scheme Administration Member Payments Rules
> 1.7 The Lifetime Allowance Rules. ...
>
> D. OVERRIDING PROVISIONS
>
> 2004 Act
>
> To the extent that any provisions of this Appendix contradict or are otherwise inconsistent with the 2004 Act and/or any regulations issued thereunder, the 2004 Act and/or such regulations (as may have been amended) shall apply."

25. Section 34(1) of the Pensions Act 1995 provides:

> "The trustees of a trust scheme have, subject to Section 36(1) and to any restriction imposed by the scheme the same power to make an investment of any kind as if they were absolutely entitled to the assets of the scheme."

26. Section 36(1) requires the trustees to exercise their powers of investment in accordance with regulations, these being the Occupational Pension Schemes (Investment) Regulations 2005 (SI 2005/3378); but the most important of these, regulation 4, prescribing the manner in which investment powers should be exercised, is disapplied in respect of schemes with fewer than 100 members. Care was taken to ensure that each of these Schemes had no more than 98 members. So far as restrictions imposed by the scheme are concerned, the most significant is the overriding requirement imposed by Appendix 1 that no benefits under the Rules are to be paid or administered in such a way as to breach Appendix 1 or otherwise prejudice the scheme's Registered Pension Scheme status for the purposes of the 2004 Act.

*Part 4 of the Finance Act 2004*

27. The payments which a registered pension scheme ("RPS") is allowed to make to its members are determined by s 160(1) of the Finance Act (FA) 2004, which provides that:

> "The only payments which a registered pension scheme is authorised to make to or in respect of a person who has been a member of the pension scheme are those specified in section 164."

28. FA 2004 s.160(2) defines "unauthorised member payment" as meaning:

> "(a) a payment by a registered pension scheme to or in respect of a person who is or has been a member of the pension scheme which is not authorised by section 164, and
>
> "(b) anything which is to be treated as an unauthorised payment to or in respect of a person who is or has been a member of the pension scheme under this Part."

29. There is then an exhaustive list of authorised member payments set out in in FA 2004 s.164(1), which provides:

> "(1) The only payments a registered pension scheme is authorised to make to or in respect of a person who is or has been a member of the pension scheme are:"
>
> (a) pensions permitted by the pension rules or the pension death benefit rules to be paid to or in respect of a member (see sections 165 and 167),
>
> (b) lump sums permitted by the lump sum rule or the lump sum death benefit rule to be paid to or in respect of a member (see sections 166 and 168),
>
> (c) recognised transfers (see section 169),
>
> (d) scheme administration member payments (see section 171),
>
> (e) payments pursuant to a pension sharing order or provision, and
>
> (f) payments of a description prescribed by regulations made by the Board of Inland Revenue."

30. 'Payment', by virtue of FA 2004 s.161(2), "includes a transfer of assets and any other transfer of money's worth." Mr Spink submits that a loan is a 'payment' within this subsection, both on ordinary principles of interpretation and by reference to sections 175 and 179, which include as one of the possible 'authorised employer payments' an 'authorised employer loan'.

31. Accordingly any payment, including a loan, by a registered scheme to a member which is not within the list at s 164(1) would be an unauthorised member payment. Of course, the PRP model seeks to avoid this consequence by providing that rather than make a payment to a member of the scheme, the scheme makes a payment to a member of a different scheme.

32. However, FA 2004 s 173, so far as material, provides that:

> "(1) A registered pension scheme is to be treated as having made an unauthorised payment to a person who is or has been a member of the pension scheme if an asset held for the purposes of the pension scheme is used to provide a benefit (other than a payment) to—

(a) the person, or

(b) a member of the person's family or household...

(5) The person who receives the benefit is to be treated as having received the unauthorised payment.

(8) The amount of an unauthorised payment treated as having been made by this section—

(a) in relation to such benefits, and in such circumstances, as may be prescribed by regulations made by the Board of Inland Revenue, is an amount determined in accordance with the regulations, and

(b) otherwise, is the amount which would be the cash equivalent of the benefit under the benefits code if the benefit were received by reason of an employment and the benefits code applied to it.

(10) In this section—

"the benefits code" has the meaning given by section 63(1) of the Income Tax (Earnings and Pensions) Act (ITEPA) 2003."

33. So if a registered scheme uses its assets to provide a 'benefit' to one of its members, that is deemed to be an unauthorised member payment. There is no direct definition of 'benefit' in FA 2004, and the Claimant submits that on a straightforward interpretation the word would include a loan. Mr Spink also points out that the "benefits code" in the 2003 Act incorporated into s 173, at least for the purposes of assessing the amount of an unauthorised payment, treats a cheap or subsidised loan as earnings.

*Unauthorised payments: the Claimant's submissions*

34. Mr Spink submits that in this case the MPVAs amount to such use of a Scheme's assets to provide a benefit to its own members because:

i) Scheme Y uses its assets to procure a loan to its own Member A, albeit from Scheme Z, by means of providing a loan to Member B of Scheme Z.

ii) The loan to Member A is a benefit.

iii) This is particularly clear given the fixed rate of 3% simple interest, compared to the 'official rate' of 4%, just for the period from 6th April 2010 to the current date.

35. The fact that the benefit is provided indirectly is irrelevant, as FA 2004 s 173 encompasses both direct and indirectly provided benefits. The phrase "*used to provide*" is of the widest possible meaning and not limited in any way, including not being limited to direct benefits. This can be seen from the following:

i) The obvious interpretation is unlimited by restrictions as to how the benefit is to be provided;

ii) The purpose behind the statute is to prevent the (untaxed) use of pension schemes to provide benefits other than those permitted under FA 2004 Part 4. A purposive interpretation therefore militates against a restrictive interpretation;

iii) The words themselves as a matter of syntax indicate this. If only a direct provision of benefit had been intended then the single word "*provides*" could stand in place of the entire phrase "*is used to provide*". The words "*used to*" necessarily indicates that the scheme assets can be deployed in a way that brings about a benefit, whether that benefit is from the scheme assets themselves or otherwise.

36. Equally, the fact that members of the reciprocal Schemes were not necessarily paired is irrelevant. The benefit is not a loan to Member A from Member B's assets. Rather, the benefit is a loan to Member A regardless of where it comes from.

37. Mr Spink gave two simpler examples to illustrate this argument:

i) Trustees of Scheme Y lend money to a complete stranger, on terms of 3% simple interest, repayable on demand but not for a minimum of 25 years. The complete stranger then lends that money to Member A of Scheme Y, on precisely the same terms;

ii) Trustees of Scheme Y lend money to a complete stranger, on terms of 3% interest, repayable on demand but not for a minimum of 25 years. The stranger uses that money to purchase property which he lets to Member A of Scheme Y, the rent being fixed at 3% of the loan per annum for 25 years.

38. He argues that the fact that the money or asset ended up in the hands of Member A via the stranger does not change the fact that this transaction is precisely the sort of transaction which s 173 is designed to catch.

*Unauthorised payments: the Defendants' response*

39. Mr Stallworthy submits that since an MPVA is never made with a member of the same Scheme from which the MPVA Amount is paid, an MPVA Amount is never paid "to" a person who is or has been a member of the scheme from which it is paid. Nor is an MPVA Amount ever paid "in respect of" a person who is or has been a member of the scheme from which it was paid. MPVA Amounts were not paid from a particular member's account: rather, they were paid from the fund of a Scheme. Moreover, the MPVA Amount paid from a scheme was not paid in order to 'buy' a reciprocal MPVA in respect of a particular member of that same Scheme. Mr Stallworthy refers to the evidence of Alan Fowler:

> "It was not necessary that members of respective schemes were twinned or even for schemes to be twinned. For the concept to work, all that was required was that the amounts 'loaned' and the amounts otherwise invested by the schemes were

> reciprocated across the various MPSs. By way of example, Member A could put £200,000 into Scheme A. Members B and C could put £100,000 respectively into schemes B and C. The reciprocation would then happen across Schemes A, B and C and not by simply 'twinning' members. It seems to me that the Claimant has misunderstood or misconceived the basis of the 'reciprocation' by looking for Member to Member twinning as central to the design."

40. Accordingly, an MPVA never involves a payment *"in respect of"* an identifiable person who is or has been a member of the Scheme from which it is paid. This is significant, because, in referring to a payment *"in respect of a person"*, the FA 2004 requires there to be *"a person"* who can be identified to be made subject to the unauthorised payments charge: see s 160(6)(a) and s 208(2)(a) FA 2004. Since an MPVA only ever involves a payment to a person who is a member of a different PRP Scheme, it does not constitute an unauthorised payment.

41. Payments can be made from a registered pension scheme which are neither unauthorised payments nor authorised payments (i.e. the classification of payments as unauthorised and authorised is not exhaustive); and which, although not authorised payments, do not attract tax charges. For example, every time the professional fees of an investment consultant are paid out of a registered pension scheme, there is a payment; but that is not sufficient to engage the FA 2004. Likewise when an investment is made with a third party who is not a member of the Scheme, that does not engage the FA 2004. The payment has to be a payment *"to or in respect of"* a member (or employer), or treated as such a payment by the provisions of the FA 2004, before it can be characterised as an unauthorised payment so as to attract a tax charge.

42. The commentary in the HMRC's Registered Pension Scheme Manual ("RPSM") provides expressly that "All schemes may make loans to third parties but loans to members (or those connected to members) are not permitted and any such loans made will be taxed as an unauthorised payment"... ... "There is no objection to a registered pension scheme making loans to third parties – i.e. persons not connected to members or sponsoring employers. Such loans are normally on an arms length basis at a market rate". Here, members of Scheme A are not 'connected' to members of Scheme B or the employer of Scheme B for the purposes of the FA 2004 (by virtue of s 161(8), "connection" is defined in accordance with s 993 of the Income Tax Act 2007). The MPVAs should be treated straightforwardly as loans to unconnected third parties, such as trigger no tax charge in accordance with this guidance.

43. After referring to s 173(1) of the 2004 Act, Mr Stallworthy's skeleton argument continues:

> "It would be stretching the wording of s 173 FA 2004 to an extreme degree to characterise the payment of an MPV Amount by Scheme A as using an asset held for the purposes of Scheme A to provide a benefit (other than a payment) to any member of Scheme A. Apart from anything else, it would be impossible to identify which member of Scheme A received the benefit from any particular MPVA entered by Scheme A with a member of

> Scheme B. There is no member-matching to allow any two MPVAs to be connected in this way. Who would bear the tax charge under s 208(2)(a)? And what would the benefit be which, under s 173(5), that member of Scheme A was treated as having received as an authorised payment? It would not necessarily correlate with the MPVA Amount invested by Scheme A, only with any MPVA Amount invested by Scheme B. There is no guarantee that the MPVA made with the member of Scheme A will secure an MPVA with any particular and identifiable member of Scheme B, because the trustees of each Scheme retain an absolute discretion as to whether or not to grant an MPVA to any member. And if any MPVA entered by Scheme B under the PRP was treated as a benefit for an identifiable member of Scheme A, surely it would not be "*a benefit other than a payment*"? Surely it would constitute a payment within the terms of s 161(2) and therefore not be within the terms of s 173(1)? All these factors militate against seeking to give s 173 such an elastic interpretation."

44. Mr Stallworthy points out that a passage in the RPSM suggests that s 173 applies to investment transactions with people connected to the scheme:

> "Various tax charges are imposed where any investment transactions entered into by the scheme (involving assets or liabilities) with people connected to the scheme are not on arm's length terms. These rules are explained [elsewhere in the Manual in these terms:] Where a transaction takes place between a registered pension scheme and a connected party in either categories A, B or C below the transaction must be made on arm's length bargain terms."

45. In any event, he submits, the MPVAs are on an arm's length commercial basis, having regard to the broader context in which they are made. Accordingly MPVAs are not unauthorised payments for the purposes of FA04.

*Unauthorised member payments: conclusions*

46. If s 173 had not been enacted, s 164 would support the Defendants' case. Mr Stallworthy is right to say that, looking at s 164 alone, the MPVA loan made from Scheme Y to B (the member of Scheme Z) is made neither "to" nor "in respect of" any member of Scheme Y. Similarly the reciprocal loan made back to A, the member of Scheme Y, by Scheme Z is made neither "to" nor "in respect of" any member of Scheme Z.

47. But I accept Mr Spink's submission that s 173 is decisive. Taking the example given above, when Scheme Y (of which A is a member) makes an MPVA payment to B (the member of scheme Z), it does so in the sure and certain hope that a corresponding payment is going to be made by Scheme Z to A; the payment to B "is used to provide" a benefit to A; and, on receiving that benefit in the form of the loan from

Scheme Z, A is to be treated as having received an unauthorised payment. The wording "is used to provide" rather than "provides" clearly indicates that indirect causation is sufficient.

48. I do not accept that any lack of precise matching between the two payments makes a difference. The PRP, as its name suggests, was established for the purpose of reciprocation. As the explanation of the PRP concept exhibited to Mr Tweedley's witness statement frankly states, "Member A is unable to access cash in existing arrangement due to Finance Act 2004 restrictions. Member A is motivated to make transfer (as advised by the introducer) to enjoy access to an equivalent reciprocal sum from Member B MPVA. The same considerations apply to Member B." [emphasis added]

49. If member A pays an amount of £50,000 (half his total investment of £100,000: see above) into Scheme Y with a view to obtaining an MPVA loan of £50,000, it is of no importance to him whether his £50,000 goes to fund a single loan to B, or is divided between several members of Scheme Z; nor whether the £50,000 which will come to him derives only from B or from several members of Scheme Z. The outcome is the same. His £50,000 is used to provide him, albeit indirectly, with a benefit, namely access to half his pension fund before his retirement, and with no strings attached except an obligation to repay £87,500 in 25 years' time.

50. The person liable to the unauthorised payment charge under s 208(2) is the recipient of the payment. So when A receives his £50,000 loan from Scheme Z, he is liable to the charge on that payment. If B received a loan from Scheme Y, B is likewise liable to be charged on the amount of that loan (whether £50,000 or some other sum).

51. The references in the RPSM to transactions with connected persons are beside the point. The benefit is not for a connected person, but for the member himself.

52. Mr Clifford argued that s 173 "is designed to cover benefits in kind, for example a residential property, and that is why it refers to benefit other than a payment. There are limits to the way in which a statutory fiction such as we find in s 173 can be stretched, and the Claimant's purported interpretation goes well beyond that limit".

53. In *DCC Holdings (UK) Ltd v Revenue and Customs Commissioners* [2011] 1 WLR 44 Lord Walker of Gestingthorpe (with whom all the other Justices agreed) approved three statements by judges in previous cases as to the proper approach to the construction of deeming provisions:

(Nourse J in *IRC v Metrolands (Property Finance) Ltd* [1981] 1 WLR 637):

> "When considering the extent to which a deeming provision should be applied, the court is entitled and bound to ascertain for what purposes and between what persons the statutory fiction is to be resorted to. It will not always be clear what those purposes are. If the application of the provision would lead to an unjust, anomalous or absurd result then, unless its application would clearly be within the purposes of the fiction, it should not be applied. If, on the other hand, its application would not lead to any such result then, unless that would

clearly be outside the purposes of the fiction, it should be applied."

(Peter Gibson J in *Marshall v Kerr* (1993) 67 TC 56):

"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."

(Neuberger J in *Jenks v Dickinson* [1997] STC 853)

"It appears to me that the observations of Peter Gibson J, approved by Lord Browne-Wilkinson, in *Marshall* indicate that, when considering the extent to which one can "do some violence to the words" and whether one can "discard the ordinary meaning", one can, indeed one should, take into account the fact that one is construing a deeming provision. This is not to say that normal principles of construction somehow cease to apply when one is concerned with interpreting a deeming provision; there is no basis in principle or authority for such a proposition. It is more that, by its very nature, a deeming provision involves artificial assumptions. It will frequently be difficult or unrealistic to expect the legislature to be able satisfactorily to [prescribe] the precise limit to the circumstances in which, or the extent to which, the artificial assumptions are to be made."

54. I accept Mr Spink's submission that in s 173(1) the words in brackets "other than a payment" must mean "other than a payment from the scheme". Otherwise the section makes no sense. Everyone is agreed that, just as payments of cash by a scheme to its own members (unless within the categories of payment authorised by s 164) are unauthorised payments, so the provision of a free or subsidised benefit in kind such as accommodation or a car is caught by s 173. If I am right in my interpretation of the words "used to provide", it follows that the indirect provision of a free or subsidised flat or car is also within s 173; and it is inconceivable that Parliament would have wished the indirect provision of a payment (including a transfer of assets or transfer of money's worth: s 161(2)) to be treated in a more favourable way.

55. When the Pensions Regulator first raised concerns about the PRP, Mr Tweedley obtained the opinion of tax counsel, Ms Amanda Hardy, who advised that the MPVA

loans were not unauthorised payments. This opinion is strictly inadmissible on the tax issue, and Mr Stallworthy accepts that it is not a legitimate aid to construction; but I have read it, and propose to treat it as an additional skeleton argument for the Defendants. Unfortunately Ms Hardy did not consider s 173, other than to say that she agreed with her instructing agent that ss 172-174 dealt with connected party transactions and were irrelevant.

56. Mr Tweedley says in his evidence that in many cases members had a desperate need for an MPVA loan. I can well believe it, but that does not assist in construing the legislation, the purpose of which is to prevent pension scheme members from spending their pension pots before retirement except where s 160 permits it. The intervention of the Pensions Regulator, described by Mr Tweedley in his witness statement as a "state sanctioned punishment [of] the members who were to benefit from something innovative and believed to be within the rules", was plainly justified.

57. I therefore conclude that the MPVA loans were unauthorised member payments as defined by s 160(2) of the Finance Act 2004. Counsel are agreed that if that is the case they were outside the powers of the Schemes' trustees and void in equity, and cannot be validated either retrospectively or prospectively by the amendments recently made to the Schemes. But since this matter may go further, and in deference to the sustained arguments of Mr Stallworthy supported by Mr Clifford, I turn to deal with the issues as to validity which do not derive from the 2004 Act; and do so on the basis, contrary to the ruling I have just given, that the MPVA loans were not unauthorised member payments within the terms of the Act.

*Were the MPVA loans "investments"?*

58. As Lloyd LJ observed in *Pitt v Holt* [2011] EWCA Civ 197 at paragraph 96, "the purported exercise of a discretionary power on the part of trustees will be void if what is done is not within the scope of the power". Clause 8.1 of each Scheme's Trust Deed gave the trustees a wide power to make investments. Mr Spink, however, argues that the MPVA loans were not true "investments" and were thus outside the scope of the power.

59. Lord Walker, giving the advice of the Privy Council in *Dominica Social Security Board v Nature Island Investment Company* [2008] UKPC 19, said that: "The word 'investment' has no very precise legal meaning, but its natural meaning in a financial context is the acquisition of an asset to be used as a source of income". Mr Stallworthy submitted, and Mr Spink accepted, that capital gain is an acceptable alternative to income, as it must be for a trust whose beneficiaries have no entitlement to an income (in contrast to the traditional occupational pension scheme, some of whose members are retired and receiving an income). In special cases, such as *Evans v London Co-operative Society* (1976) [1999] 55 PBLR 24, it may be justifiable to obtain less than a full commercial rate of interest. And of course trustees may properly balance rate of return and risk.

60. As the *Dominica Social Security Board* case itself illustrates, it is important not to confuse *vires* with prudence. It would not be difficult to answer the question of whether a fixed term loan for 25 years, with no return except a capital gain at the end of the term corresponding to 3% simple interest per year, and no security against the

borrower's death, insolvency or disappearance, is or is not a prudent investment. But it is not the question I have to decide.

61. In *Khoo Tek Keong v Ch'ng Joo Tuan Neoh* [1934] AC 529 the Privy Council held that a clause giving the trustee of a will an absolute discretion to choose such investments as he thought fit did not entitle him to make an unsecured personal loan, even at interest. The editors of *Underhill and Hayton on Trusts,* describe the decision as "an old case of doubtful authority nowadays", and it must be said that the relevant part of the judgment consists of a single sentence with no reasons; but a judgment of Lord Russell of Killowen with the concurrence of Lords Blanesburgh and Tomlin cannot be dismissed out of hand. *Underhill and Hayton* comment that "if a secured loan is an investment it is difficult to see why an unsecured loan is not also an investment that could form part of a well-balanced portfolio if balanced by little or no-risk investments, especially where the loan was an urgent one made in the subsequently unfulfilled expectation that security would be provided". This cannot, of course, be said of the MPVA loans.

62. In *re Peczenick's Settlement* [1964] 1 WLR 720 trustees held property "for the purpose of investing such funds in any shares stocks property or property holding company as the trustees in their discretion shall consider to be in the best interest of Shiela". Buckley J held at 723:

> "Taking clause 1 by itself, it appears to me that the clause authorises the trustees to invest in any shares, any stock, or any property. It must, of course, be property of a kind capable of being treated as an investment, not property which is acquired merely for use and enjoyment. Apart from that, however, it seems to me that clause 1 places no restriction on the discretion of the trustees, beyond saying that the investments must be investments in stocks or shares or something which can properly be described as property. The clause would not, I think, authorise investment merely on personal security." [emphasis added]

63. These two cases indicate that an unsecured personal loan is incapable of being an "investment" within the meaning of clause 8.1 of the Schemes' Trust Deeds.

64. Mr Spink alternatively argues that even if an unsecured personal loan is capable of being an "investment" for these purposes, in the present case the MPVA loans were not in fact "investments". Notwithstanding the 3% rolled-up interest rate, they were not made for the purpose of obtaining a return for the lender (such as member A in Scheme Y), whether by way of income or capital gain. Rather they were made to a member of another Scheme for the purpose of procuring a reciprocal long-term loan from that Scheme to A. I accept this submission. I would characterise the purpose of the PRP as being not investment but disinvestment. The MPVA loans were accordingly outside the scope of the power of investment in the Schemes.

*No exercise of the trustee's discretion*

65. Mr Spink submitted, referring to the decision of Mervyn Davies J in *Turner v Turner* [1984] Ch 100, that there is no evidence that the schemes' trustees exercised any real discretion when considering applications for MPVA loans, and that the loans are therefore invalid on this further ground. This issue only surfaced in the Claimant's skeleton argument: it was not raised expressly either in the Claim Form or in the Claimant's evidence. In the circumstances Mr Stallworthy and Mr Clifford understandably objected to my ruling on it, and I consider their objection well founded.

*Fraud on the power*

66. The final string to Mr Spink's bow, if I am wrong both on s 173 and on the meaning of "investments", is the argument that the MPVA loans constituted a fraud on the power of investment. This time-honoured but (at least to the layman) misleading phrase does not connote dishonesty. It was explained by Lord Parker of Waddington in in *Vatcher v Paull* [1915] AC 372 at 378:

> "It merely means that the power has been exercised for a purpose, or with an intention, beyond the scope of or not justified by the instrument creating the power. Perhaps the most common instance of this is where the exercise is due to some bargain between the appointor and appointee, whereby the appointor, or some other person not an object of the power, is to derive a benefit. But such a bargain is not essential. It is enough that the appointor's purpose and intention is to secure a benefit for himself, or some other person not an object of the power."

67. *Thomas on Powers* puts it in this way (at paragraph 9-01):

> "Thus there are two basic elements in a fraudulent exercise of a power first, a disposition beyond the scope of the power by the donee, whose position is referable to the terms, express or implied, of the instrument creating the power; and, secondly, a deliberate breach of the implied obligation not to exercise that power for an ulterior purpose. The first element is common to both a fraudulent and an excessive execution. It is the second element which distinguishes a fraud on a power."

68. *Thomas* goes on to emphasise (at paragraph 9-04) that the scope and purpose of a power must be determined objectively:

> "The true intention of the donor of the power as to its scope and purpose must, of course, be ascertained from the instrument creating the power, even where the donor and the donee are the same person."

69. The instrument in question in this case is each scheme's Trust Deed and Rules. As drafted, and before any amendment, these are standard form documents permitting "investments" but saying nothing about the PRP or MPVA loans. The issue between the parties on this aspect of the case is whether other evidence such as Ark's

promotional literature can be admitted to demonstrate that the true intention of the donor of the power of investment was to facilitate the PRP and MPVA arrangement.

70. Both sides cited and relied on the two leading modern decisions of the House of Lords on what may be taken into account in construing a contract or a trust deed. Lord Hoffmann gave the leading speech in each of them and referred back to the first in the second, *Chartbrook Ltd v Persimmon Homes Ltd* [2009] 1 AC 1101, where he said (at paragraph 14):

> "There is no dispute that the principles on which a contract (or any other instrument or utterance) should be interpreted are those summarised by the House of Lords in *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 WLR 896, 912–913. They are well known and need not be repeated. It is agreed that the question is what a reasonable person having all the background knowledge which would have been available to the parties would have understood them to be using the language in the contract to mean."

71. The House went on, however, to affirm the long-established exclusionary rule (set out, for example, in *Prenn v Simmonds* [1971] 1 WLR 1381) prohibiting the use as an aid to construction of "evidence of what was said or done during the course of negotiating the agreement for the purpose of drawing inferences about what the contract meant" (paragraph 42 of *Chartbrook*); or, in the wording used in the *Investors' Compensation Scheme* case, "the previous negotiations of the parties and their declarations of subjective intent".

72. I consider that the Claimant succeeds on this issue essentially for the same reasons as it does on the second issue. The powers of the trustees are to make "investments" as set out in Clause 8.1 of each Trust Deed. The Deed and Rules must be objectively construed without reference to external documents showing the subjective intentions of the creators of the PRP. The MPVA loans were beyond the scope of their powers, and made for an ulterior purpose. The fact that everyone involved with the transactions *wished* to validate MPVA loans does not prevent the loans from being a fraud on the trustees' powers.

*The amendments to the schemes' trust deeds and rules*

73. On 13 October 2011, the day when the Defendants' witnesses signed their witness statements, amendments were made to the terms of all six Schemes to add the following:

<u>New Clause 8A - 'Maximising Pension Value Arrangement'</u>: *"Without prejudice to any other powers they may have, the Trustees may at their discretion enter into one or more transactions involving the funds of the Scheme with one or more members of any other Registered Pension Schemes, on such terms as the Trustees at their discretion shall decide, which terms may include (but shall not be limited to) terms as to any rate of interest or other investment return, duration or maturity provisions."*

Addition to Clause 10 - Scheme Expenses: *"The Trustees may pay to one or more third parties any fees, costs, charges, commissions or other amounts including but not limited to those which the Trustees shall in their absolute discretion determine are referable to or connected with a Member's admission to Membership of the Scheme or a Member's transfer in or other payment to the Scheme."*

74. As recorded above, counsel were agreed that if (as I have found) the MPVA loans were unauthorised member payments, they cannot be validated either prospectively or retrospectively by new clause 8A. This follows inexorably from the overriding requirement set out in Clause 16 and Appendix 1 that nothing must be done to infringe the scheme's registered status under the 2004 Act.

75. If I am wrong in ruling that the MPVA loans were unauthorised payments, I would still hold that new clause 8A cannot validate MPVA loans, even prospectively. In *Hole v Garnsey* [1930] AC 472 the House of Lords held that a power to amend (in that case, the rules of a society registered under the Industrial and Provident Societies Act 1893) cannot be used to make an amendment which was outside the "reasonable contemplation of the parties" to the contract containing the power when that contract was made. Like "fraud on the power", the expression "reasonable contemplation of the parties" is a term of art, and does not mean what it may appear at first sight to mean. In *PNPF Trust Co Ltd v Taylor and others* [2010] EWHC 1573 (Ch) Warren J considered it in the context of amendments to a pension scheme. He said (at paragraph 144):

> "The "reasonable contemplation" of the parties, or rather what can "reasonably be considered to have been within the contemplation of the parties", imports an objective test. It is not, in my view, relevant to know what the parties did or did not actually consider. I am not, for instance, concerned with what the directors of any of the CHAs discussed in their boardroom or considered with their lawyers. That is consistent with descriptions of the restriction on the scope of a power to alter the objects or purposes of the trust; the amendment must not change the whole substratum of the trust (see in an analogous situation *Re Ball's Settlement Trusts* [1968] 1 WLR 899 and also *Kearns v Hill*) or its basic purpose (see *Bank of New Zealand v Board of Management of New Zealand Officers' Provident Association* [2003] UKPC 58)."

76. Here each Scheme is described, in the first recital in the deed, as a pension scheme within s 150 of the 2004 Act. The purpose of such a scheme is to provide benefits to or in respect of its members on retirement, death, reaching a particular age, the onset of serious ill-health or incapacity, or in similar circumstances. An amendment to allow unsecured loans to non-members in order to procure reciprocal loans to members alters the basic purpose of the scheme, or, as Warren J put it, the whole substratum of the trust.

77. The position is even clearer as regards retrospective effect. In *Bank of New Zealand -v- Board of Management of the Bank of New Zealand Officers' Provident Association* [2003] UKPC 59, [2003] OPLR 281 at paragraph 26 Lord Walker said:

> "In the courts below the Board of Management's power to make a retrospective amendment was dealt with as a separate topic. But before their Lordships it was rightly conceded that this topic is merely a reflection of, or another (and possibly less helpful) way of putting, what is essentially the same point as to the scope of the power of amendment. Modern authority.... has recognised that when the law raises a presumption against the retrospective operation of an enactment or a disposition (including a rule change), it is concerned with fairness in the circumstances of the particular case, rather than with the application of some general formula. In the amendment of pension scheme rules, back-dating (that is, deeming a change of the rules to have been made at a date earlier than the date of the actual change) cannot be used as a device so as to rewrite history or validate an amendment which would otherwise be beyond the scope of the power of amendment. But if the substance of what is proposed is within the power, back-dating will not by itself lead to invalidity ... "

78. New clause 8A is an attempt to validate retrospectively acts which, at the time they were committed, were breaches of trust. As such it is, as the Claimant submitted, a device to rewrite history and accordingly ineffective.

79. In the case of the addition to clause 10 (which allows payment of fees or commission to introducers, without specifying a figure) I do not consider that there is anything objectionable in principle about such an amendment with prospective effect; whether 5% is a proper figure is not a question I am asked to determine. But, as in the case of Clause 8A, the amendment cannot validate commission charges retrospectively. If the 5% fees were paid out in breach of trust, it cannot be in the interests of the scheme members to validate such a breach after it has been committed.

*Other questions raised in the Claim Form*

80. Counsel were agreed that in the event of my deciding that the MPVA loans were invalid as being unauthorised payments, I should declare that they are void in equity; that the trustees are not estopped as against the members from denying the validity of the loans; and that further MPVA loan payments from the schemes cannot lawfully be made. The other consequences of my decision will have to be dealt with if necessary in other proceedings: in particular, a separate Part 7 claim is on foot in which Dalriada seeks to recover the sums paid out by way of commission to introducers, which exceed £1 million. I will hear counsel on the form of order which is appropriate when they have considered the draft of this judgment.