A HIGH COURT OF JUSTICE (CHANCERY DIVISION)—
27 APRIL AND 14 JUNE 2001

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COURT OF APPEAL—5 JULY AND 18 SEPTEMBER 2002

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Venables and Others v. Hornby (H.M. Inspector of Taxes)[1]

Income tax—Pension schemes—Retirement—Normal health—Payments out of pension schemes funds—Pension scheme providing for payments to persons who retired early in normal health—Recipient had ceased to be full-time and executive director, but was unpaid non-executive director—Recipient overweight, and having high blood pressure and mild diabetes—Whether payments chargeable to income tax because they were not paid in course of payment of a pension—Whether the recipient had retired—Whether he had retired in normal health—Whether, if payment not authorised under scheme, recipient not beneficially entitled to it and therefore not chargeable to tax—Income and Corporation Taxes Act 1988 ss 590, 591, 600 and 612.

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V was a substantial shareholder, in his own right and as settlor and trustee of a family trust, in VH, the parent company of a group engaged mainly in property development. Up to 1993 he had, as executive director and chairman, worked about 30 hours a week. After the retirement in 1993 of the managing director, V worked nearly 50 hours a week, running the day to day business as well as making strategic decisions.

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By June 1994 V was anxious to give more of the responsibility to his two children and to S, and he had some concern about his health: he was 21 stone, and had high blood pressure and mild diabetes. S became managing director and V's daughter became the company secretary. A board minute recorded that V was "retiring as an executive director on 30 June 1994 to pursue other interests but will continue as an unpaid non-executive director". After June 1994 V spent much of his time in North America, but gave some help, usually by telephone, in the running of the company.

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Under VH's pension scheme normal retirement age was 60, but the trustees had power to award an immediate pension to a scheme member "who retires in normal health at or after the age of 50". Between July and August 1994 the scheme paid three sums, in aggregate £580,591 to V, who was 53.

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V appealed against assessments to income tax for 1994–95 made under s 600 Income and Corporation Taxes Act 1988, on the footing that the payments were

(1) Reported [2001] STC 1221; [2002] EWCA Civ. 1277; [2002] STC 1248; [2003] UKHL 65.

not expressly authorised by the rules of the scheme, the payments having been made "otherwise than in the course of payment of a pension". The trustees appealed against a related determination under Regulation 49 of the Income Tax (Employments) Regulations 1993. The Special Commissioners (SpC 0265) dismissed the appeals, holding that V had retired, but that he had not retired "in normal health". A B

V and the trustees appealed. They did not pursue a contention relating to the Human Rights Act 1998. Reference was, however, made in the High Court to the definition of "relevant benefits" in s 612(1) of the 1988 Act, *viz*. any pension "given or to be given on retirement or on death, or in anticipation of retirement, . . . or to be given on or in anticipation of or in connection with any change in the nature of the service of the employee in question". C

The Chancery Division held, allowing the appeals of V and the trustees, that the payments were made "in the course of payment of a pension" and were not chargeable to tax under s 600, because:— D

(1) since the trust deed and rules were drafted against the background of the legislation and the need to obtain Revenue approval, they must be construed against the background of the legislation; no assistance was to be derived from the references in the legislation to "employee", "service" and "retirement"; while s 612(1) did not assist in the meaning of "retirement", it clearly showed that a change in the nature of the service of an employee can qualify the employee to benefits, and that an exempt approved scheme may lawfully provide a pension on early retirement in such circumstances; E

(2) the trust deed and rules are to be given a practical and purposive construction; F

Re Courage Group's Pension Schemes [1987] 1 WLR 495, *Mettoy Pension Trustees Ltd.* v. *Evans* [1990] 1 WLR 1587 and *Harris* v. *Lord Shuttleworth* [1994] ICR 991 considered;

(3) there can be no principle that, when a person changes from being a paid executive director to being an unpaid non-executive director, that person does not "retire", it is a matter of fact and degree as to whether a person has retired, which connotes withdrawing from active work; mere reduction in workload is not retirement; but the fact that a person continues to be a director does not establish that that person had never retired; G H

(4) there was sufficient evidence for the Special Commissioners' decision on the facts that V had retired, and there were no grounds for interfering with it;

(5) the expression "in normal health", in the context of a pension scheme trust deed, must mean "normal" by reference to some standard, and the only standard which could reasonably be applied was fitness to do the job; I

(6) the Special Commissioners could not reasonably have arrived at the conclusion that, for the relevant purpose, V was not in normal health; V was spending 50 hours a week as an executive director at the time of his resignation, which suggested strongly that he was fit to do the job, and there was no evidence

A that he was unfit to do it; there was no evidence to support the finding that even in the abstract V was not in normal health; high blood pressure and mild diabetes were common conditions in overweight middle-aged men, and there was no finding that V's health was abnormal.

Per curiam: if each and every one of the following conditions is fulfilled, then B there is no taxable payment for the purposes of s 600: that the payment is in breach of trust, that the recipient is accountable to the trustees as an actual or constructive trustee, and that the recipient is able and prepared to account to the trustees.

The Crown appealed, but did not pursue the contention that V was not "in C normal health".

The Court of Appeal held, allowing the Crown's appeal, that:—

(1) the payments were not authorised by the scheme because V had not retired, as:

D (a) the question whether V retired was one of construction, not one of fact and degree;

(b) the terms of the scheme showed they were intended to be construed in the same sense as in the relevant legislative provisions;

(c) in view of the distinction in s 612(1) between "benefits given on retirement" and "benefits given on any change in the nature of service", the E only meaning which could be given to "retirement" was "cessation of service"; as "employee" included a director of a company, circumstances in which a director continued to hold office might involve a benefit given on a change in the nature of service, but could not involve a benefit given on retirement;

F (2) s 600 applied to the payments, as the charge to tax under s 600 arose only where, as here, the payment was unauthorised and in breach of trust, and otherwise the provision would be self-defeating; it was impossible to limit the scope of s 600 in the way suggested by the High Court Judge (see the *per curiam* passage above);

Hillsdown Holdings plc v. *Commissioners of Inland Revenue* (1999) 71 TC G 356; [1999] STC 561: distinguished.

V and the trustees appealed.

Held, in the House of Lords, allowing the appeal of V and the trustees (Lord Walker of Gestingthorpe dissenting), that V was both a paid employee and an H unpaid director of VH on 30 June 1994, and that, on the true construction of the trust deed, he retired from service as an employee on that date even though he continued to be an unpaid non-executive director thereafter; in particular:

(1) (Lord Scott of Foscote disagreeing), there was abundant evidence to support the Special Commissioners' conclusion that V was an employee (in the I ordinary sense of that term) of VH, and the absence of a written contract was neither surprising nor conclusive;

(2) the expression "directors and employees" in the trust deed could not sensibly be confined to persons who were both employees and directors, but meant persons in the service of the company whether as employees or directors, and "retire" therefore meant "retire from the service of the company whether as employee or director"; it was therefore not necessary that a member who was an employee and a director should retire from both positions;

per Lord Millett: it was most unlikely that the trust deed was not intended to cover early retirement in ill health, so the words "in normal health" should be treated, not as words of limitation, but as words of exposition, and, read in that way, they referred to a member "who retires (even in normal health) at or after the age of 50".

Decision [1]

1. These are two distinct but related appeals. The first is by David John Venables against a Sch E assessment made on 6 April 1994 in respect of three payments to him by the trustees of the Fussell Pension Scheme totalling £580,591, which the Crown say were not authorised by the terms of the Scheme and are chargeable under s 600 of the Income and Corporation Taxes Act 1988. The second appeal is by the trustees of the Scheme against a determination under Regulation 49 of the Income Tax (Employments) Regulations 1993 in respect of the basic rate tax deductible from same payments. Both stand or fall together.

2. The basic issue, put shortly, is whether Mr. Venables retired on 30 June 1994 within the meaning of s 600. Other issues arising are a mixed one as to jurisdiction and the practice of the Pension Schemes Office (the PSO), one on trust law and one on the Human Rights Act 1998. To a substantial extent there were agreed facts but, in addition, there was oral evidence from Mr. Venables and from Mr. J C Hayward, a former member of the PSO, and now a pensions practitioner.

Mr. Venables's evidence

3. I take the facts with regard to Mr. Venables first. Though obviously a man of much experience in business, and one who would probably be described as "tough", Mr. Venables struck me as defensive, not pleased at having to give evidence, and ill at ease in doing so. It is uncontested that Mr. Venables, who is now 59—he will be 60 on 13 December 2000—is and was a substantial shareholder in Ven Holdings Ltd. (Ven Holdings), having in his own right 20 per cent. of the shares and, as settlor and a trustee of his family discretionary trust, the remaining 80 per cent. Ven Holdings has a number of subsidiaries and the main business of the group is described as "property development and selected aspects of the construction industry". From 1991, the group comprised ten

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[1] Reported [2000] STC (SCD) 579.

A companies and had gross assets of some £7m, though by 1994 it had contracted to eight companies with assets of some £4m.

4. Mr. Venables was a carpenter by trade and in the early days had worked on the sites, though he has not done so for many years. Overall, Mr. Venables worked in Ven Holdings for upwards of thirty years, and had for some time been B an executive director and the chairman of the company, in which capacity he worked about 30 hours a week. On 31 March 1993, the group's managing director retired and Mr. Venables's workload increased so that he then worked nearly 50 hours a week. Before that, he had been occupied for the most part in making strategic decisions for the activities of the group, but now he became responsible for its day to day running, arranging the finances, costing work and C recruiting staff.

5. A year passed, and Mr. Venables was anxious to give more of the responsibility to his children Steven and Paula, and a man called Luke Singleton. By 1994, a little over twelve months since the last managing director had retired and Mr. Venables had increased his workload, he had already decided that the D time was ripe for him to do this, and he ceased to undertake all the responsibilities that he had had since 31 March 1993: Mr. Singleton became managing director (which post he continued to fill until 1998, when Steven Venables took over); it is not clear what Steven did in the meantime, but Paula Venables became company secretary on 23 June 1994. The board minutes of 23 June 1994 record that "L G Singleton is to be elected to serve as Managing Director for a trial period of six months with Miss P J Venables appointed as Company Secretary".
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6. I find that Mr. Venables was not formally the "managing director": the minutes of the board on 23 June 1994 recorded only that Mr. Venables was "retiring as an executive director on 30 June 1994 to pursue other interests but will continue as an unpaid non-executive director" : there is no minute of his appointment as managing director, in contrast to that which appointed a F managing director from 30 June onwards, and my conclusion is that Mr. Venables stepped into the gap left on 31 March 1993 without any particular formality. That he performed the functions which would have been performed by a managing director if there had been one, I do not doubt, but there is no evidence of his appointment to that office, even though Regulation 84 of Table A was applicable to the company and provided that such an office might be held. G After 30 June 1994, Mr. Venables was an unpaid non-executive director, and ceased to be an employee, not having even an oral contract.

7. The question of Mr. Venables's health is difficult. Mr. Venables stated that he is 21 stone and a sufferer from diabetes, and had had three heart attacks. I understood this to have been the case by 30 June 1994, though when the question H whether he had retired in "normal health" was seen to be material (I refer to why below) it was stated—and not challenged by Mr. Brennan—that Mr. Venables's heart attacks occurred after June 1994, as did his diabetes. My note of Mr. Venables's oral evidence in re-examination is that he said, in connection with his decision to go in June 1994:

> "I had worked for myself since I was fifteen; I worked for thirty six I years; I was having heart problems and wanted to slow down and leave it all to the children; I had three heart attacks; I am twenty one stone and diabetic."

I note that 15 plus 36 is 51, and that Mr. Venables was in fact 53 by June 1994, so he must have been referring to his condition at least in early 1994 if not before. A

8. With some hesitation, therefore, I accept the clarification—even though it was made only through counsel—that the three heart **attacks** occurred after 30 June 1994, but I find that concern about his health was part of Mr. Venables's reason for wanting to pass on his newly acquired responsibilities after so short a time, and when he was only 53, and that he was not then in "normal health". B

9. On 23 June, Mr. Venables wrote to his pension consultant that although he had decided to retire from employment with the Fussell Group from 30 June he hoped to be involved in one or two new business ventures outside the property companies, and that he wanted to take most of his lump sum from the Scheme in the form of property. He explained in evidence that that was because there was little cash in the scheme and it was pointless to sell properties when he could have the same value without doing so. (I note that Mr. Venables did not say in his letter that he was "retiring from service as managing director" as incorrectly asserted in the Agreed Statement of Facts.) C D

10. As to his activities following 30 June 1994, Mr. Venables spent a large proportion of his time in North America, buying a house in Florida in May 1996, though from time to time returning to the UK. In spite of the distance of time and place, Mr. Venables nonetheless continued to be interested in the running of the company, since he remained—either on his own account or as a trustee—the major shareholder. He tried to guide the family in what they were doing: they could telephone him to seek advice on a wide range of matters—how they should deal with the bank manager? what rates should they pay? how best to twist his arm? would this or that building be likely to be a good acquisition? Mr. Venables had a store of experience and business sense on which his family were glad to draw. E F

11. It was all usually done by telephone, and Mr. Venables received no remuneration from the company to recompense him for his interest in its fortunes. As a trustee of the family trust, and as the originator and hitherto the mainstay of the business, it was natural for him to take that interest, and as trustee he was actively involved in the trust's investment deals. He might tip the company off about a good deal, or even on occasion cut a bargain on his own account, because he owned a small property company of his own. It was in his blood, and he did not lose interest in his lifetime's work in a single moment. G

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12. But Mr. Venables no longer went to the sites as he had done before June 1994, or normally attend at the office. As a non-executive director, and still ultimately in control through shareholdings, Mr. Venables was useful, conscientious and available, even addressing himself to particular matters such as the adequacy of credit control; he did not, however, run the company and could in his personal circumstances scarcely have done so. As I have noted already, his health was not good, and during the period we are concerned with he had three heart attacks, and he was for the most part physically absent—not an hour's drive from the business, but on the other side of the Atlantic. It was shown that on one occasion after June 1994 he had signed off the company's accounts, but he didn't normally do so. I

A 13. I find therefore that Mr. Venables

(i) was not in normal health on 30 June 1994,

(ii) did not retire from the office of managing director, because he had never been appointed to it, but

(iii) did retire from employment with the company and from normal active service on its behalf.

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The Fussell Pension Scheme

14. Before considering Mr. Hayward's evidence, I must turn to the details of the Fussell Pension Scheme and to the statutory provisions bearing on it.

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15. The Scheme was established on 25 September 1980 by a trust deed made between Fussell Estates Ltd., Mr. Venables and Neill Alexander Denton, to provide relevant benefits for directors and employees of Fussell Estates Ltd. It was an "approved" scheme for the purposes of Chapter II of Part II of the Finance Act 1970, but it ceased to be approved on 5 August 1994 because it did D not amend its rules to comply with the Retirement Benefits Schemes (Restriction on Discretion to Approve) (Small Self Administered Schemes) Regulations 1991. The payments assessed in this case were all made before that date—in the last case, one day before.

16. Clause 1 of the trust deed established the Scheme on the basis of the E provisions of the deed, which are contained in schedules to it, and "the Rules made hereunder". The Rules are defined in Sch A by reference to clause 2 of Sch D, which provides:

"2. Upon an employee being offered membership of the Scheme a letter with an appendix attached setting out the terms conditions contributions (sic) to be made by the Employer and the Employee F respectively and benefits to be provided will be drawn up in a form acceptable to the Commissioners of Inland Revenue and signed so as to indicate acceptance by the Employee and by an authorised signatory of the Employer Upon acceptance the said letter with the appendix attached will be the Rules applicable to such member and may be superseded in whole or in part by subsequent letters duly signed and accepted in the manner stated G above The Rules with this Deed will be binding (although the Rules be not under seal) on the Member the Employers and the Trustees." [there is no punctuation in this text]

17. The Scheme Rules applicable to Mr. Venables include the following:—

"2 You will normally retire from the Company's service on 13 H December 2000, your normal retirement date when you will be aged sixty years and you will have been a member of the Company for more than 20 years. . . . You may elect to take part of your capital sum in the form of a tax free cash sum up to a maximum of 150% of your final remuneration as defined in the trust deed. . . ."

"5 The following paragraphs describe the general conditions relating I to the payment of your benefits. However, it is the Trust Deed which governs these conditions and it will always take precedence over this Rule.

(a) With the Company's consent you may retire at any time after age 50. At the date of actual retirement, your capital sum in the Scheme would be released to provide reduced benefits. An immediate pension is an optional alternative to the benefits described in Rule 4 above."

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18. Particularly in view of the opening words of Rule 5, one then refers to the trust deed in connection with early retirement. Under clause 2 of Sch F to the deed, the trustees had discretion to award an immediate pension to a member of the Scheme "who retires in normal health at or after the age of fifty", and under clause 5(b) of that Schedule "before payment of a pension commences . . . the Trustees may . . . commute part of such Member's . . . pension for a lump sum". The power to commute is therefore dependant on the prior award of the pension, and that—to be in accordance with clause 2—is dependant on the member (a) having "retired" and (b) having done so "in normal health".

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19. Neither of these expressions used in Sch F is defined, but clause 2 of Sch B to the deed provides that:—

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"Subject to the powers to be exercised by the Employers as herein expressed the Trustees shall have full power to determine in consultation with the Founder [originally Fussell Estates Ltd. but Ven Holdings Ltd. at the relevant time] whether or not any person is entitled from time to time to any benefit or payment in accordance with the Scheme and in deciding any question of fact they shall be at liberty to act upon such evidence or presumption as they shall in their discretion think sufficient although the same be not legal evidence or legal presumption Subject as aforesaid the trustees shall also have power to determine all questions and matters of doubt arising on or in connection with the Scheme and whether relating to the construction thereof or the benefits thereunder or otherwise." [there is no punctuation in this text]

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20. Clause 2 of Sch B must be construed strictly since it is capable of affecting adversely the interests of the beneficiaries of the Scheme and, to an extent, seeks even to oust the jurisdiction of the court. Whether it is successful in doing so it is not for me to decide and, in any event, it is not necessary in this case to do so.

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21. The first part of the clause refers to entitlements, whereas the immediate pension on early retirement provided for under Sch F clause 2, and the lump sum paid under Sch F clause 5(b), are discretionary and are therefore not entitlements as such. But even if that is wrong, the first part of the clause correctly construed does no more than provide the trustees with the power to make ordinary decisions in the conduct of the pension fund, but it does not purport to make those decisions unassailable.

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22. Nor does the second part of the clause. There is no evidence that the trustees have sought to exercise the power to determine any "questions and matters of doubt arising", and it was not suggested that they had done so. Nor can the exercise of this power be inferred merely from the fact of the award being made to Mr. Venables, because there is no evidence that the trustees thought that their action was controversial or that it would not meet with Revenue approval. It will be seen below that the Appellants' case includes the claim that the pensions

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A industry would have seen nothing exceptional or exceptionable about the early retirement lump sum award to Mr. Venables: whether that is true or not, that could not be asserted as a matter of fact consistently with a claim that the trustees had made a determination about a matter in dispute.

23. As to the Rules, I find it difficult to see why they make provision in a B particular matter which is at odds with that in the trust deed—the relevant difference in this case being that they appear to envisage early retirement generally, and make no reference to good or ill health, but the trust deed refers only to early retirement in normal health. There is nothing in either place to provide for early retirement in poor health, except in so far as it is implicit in Rule 5. Since the only two provisions about early retirement are those I have cited, and C since Rule 5 which deals with early retirement is—alone among the rules—clearly expressed to be subject to the deed "which will always take precedence over this Rule", I have to conclude that the restrictive wording of clause 2 of Sch F cuts down the apparent width of Rule 5. Early retirement on the grounds of ill health is apparently a *casus omissus*.

D **Legislation**

24. Section 600 of the 1988 Act provided, so far as material:—

> "(1) This section applies to any payment to or for the benefit of an employee, otherwise than in course of payment of a pension, being a payment made out of funds which are held for the purposes of a scheme E which is approved . . .
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> (2) If the payment is not expressly authorised by the rules of the scheme or by virtue of paragraph 33 of Schedule 6 to the Finance Act 1989 the employee . . . (whether or not he is the recipient of the payment) shall be chargeable to tax on the amount of the payment under Schedule E for the year of assessment in which the payment is F made.
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> (4) References in this section to any payment include references to any transfer of assets or other transfer of money's worth."

25. Section 612 of the 1988 Act defined "employee" and "director" and it was common ground that Mr. Venables was a director both before and after 30 G June 1994, and an employee before that date. So far as it is in dispute, the section provides:

> "'employee'—(a) in relation to a company, includes any officer of the company, any director of the company and any other person taking part in the management of the affairs of the company,"

and

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> "'service' means service as an employee of the employer in question and other expressions, including 'retirement', shall be construed accordingly;"

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Mr. Hayward's evidence

26. There was no case cited deciding the meaning of retirement in this precise context. Mr. McDonnell submitted that the word should not necessarily be given the meaning it has in the legislation, but that it should however be construed in accordance with the commonly accepted understanding of the PSO's practice. That is because such practice was likely to have been in the mind of the draftsman of the trust deed, whose recitals make it clear that the intention was to establish pension provisions acceptable to the Inland Revenue; the trustees who administered it, moreover, would seek to do so on the same basis. It was said also to be material to a Human Rights argument which I will come to later.

27. Mr. Brennan strongly opposed the admission of Mr. Hayward's evidence about this on the ground that it could not be relevant to matters within the jurisdiction of the Special Commissioners, namely the correct interpretation of the statute and its application to the facts of the case. If it proved anything, Mr. Hayward's evidence might show a legitimate expectation that a certain practice would be followed but, if it did show that, the issue would be one for judicial review alone. In support of that he cited the observations of Sir Richard Scott V.C. in *Steibelt* v. *Paling* [1999] STC 594, at pp 602 to 603, Jonathan Parker J. in *Hatt* v. *Newman* [2000] STC 113, at pp 120 to 121, and Leggatt L.J. in *Koenigsberger* v. *Mellor* [1995] STC 547, at pp 553 to 554.

28. These principles are too well known for it to be useful for me to enter any discussion of them here and indeed they were not contested by Mr. McDonnell. I decided, nonetheless, to hear Mr. Hayward's evidence and to consider in the light of it whether it could have any bearing on the construction of the trust deed or the Human Rights argument. In the event I think it is really no help at all on those issues, but I will indicate what he said.

29. Mr. Hayward worked in the Superannuation Funds Office, the predecessor of the PSO, from December 1979 to May 1988, as a senior executive officer until 1986 and then as a principal. From June 1986 until May 1988 when he left, Mr. Hayward was responsible for the day to day policy on small self-administered pension schemes. He is now a pensions consultant familiar with PSO practice on small self-administered schemes and is of considerable professional standing in that field. Mr. Hayward says that between 1979 and 1988 many requests were made to the PSO to agree the mode of early retirement in individual cases, because schemes were anxious not to make payments which would subsequently be disallowed.

30. The requests were usually "although not always" accepted if ill-health was the cause of a reduced role or where a person continued as a non-executive director, but "each director's early retirement request was treated on its merits". As practitioner, Mr. Hayward believed that the PSO's practice continued after he left that office in1988, and he exhibited two pieces of correspondence—neither of which was his own—to support that belief. For some years before 1994, he said that the practice was so well established that "where a director fully resigned or became a non-executive director after age 50 early retirement benefits were often taken without an approach being made to the PSO beforehand".

A 31. Reference was made then to an internal Revenue manual called PSI 6.4.27 published in the summer of 1996 for the policy of the PSO which, Mr. Hayward said, had been consistently the same since his time there. That was said to confirm that where a director retired from an executive appointment before retiring as a director, an early retirement pension could be taken after age 50 and a new scheme operated for post-retirement earnings, so that the individual would B have as it were parallel existences, one retired and the other one somewhat active and moving towards a separate "normal" retirement date. Lastly, Mr. Hayward commented that he believed that PSO practice had changed in late 1995, but declined to speculate as to why.

32. It is no disrespect to Mr. Hayward, who I regarded as an entirely C truthful witness, and doubtless a specialist in his field, to say that his evidence was necessarily sketchy and speculative and could not possibly establish as a fact everything relevant to what the PSO's practice was, or how cases were dealt with, or whether there were exceptions and if so on what grounds. Mr. Hayward stopped short of saying that if he had been dealing with this case he would not have sought the PSO's clearance before Mr. Venables received his payments, and D he accepted that much of his experience of what the PSO did was second hand.

33. Whether a witness summons issued to an appropriate Revenue official, with an application to treat him as hostile, would have disclosed better or more comprehensive evidence I cannot say but, in my view of it, the most that Mr. Hayward's evidence could do would be to support a *prima facie* case of legitimate E expectation (though I say nothing about that), and was not apt to assist in the construction of the trust deed. The burden of establishing that a course of practice existed, but was not followed in this case for no good reason, falls on the taxpayer and it has not been discharged: it is not for the Revenue to prove their innocence of the charge. I return below to the Human Rights argument, which this evidence was also designed to support.

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The Authorities

34. Mr. McDonnell relied on a number of decisions to support the claim that Mr. Venables had "retired" on 30 June 1994, in particular, *Mettoy Pension Trustees* v. *Evans* [1990] 1 WLR 1587. That case concerned a number of issues G arising on the winding up of a company and did not involve the questions which arise here, but it is relied upon for the comments made about the manner in which pension scheme trusts should be interpreted.

35. Thus, at p 1610, Warner J. adopted the comment of Millet J. in an H earlier case (*in re Courage Group's Pension Schemes* [1987] 1 WLR 495, at p 505) that "its provisions should wherever possible be construed to give reasonable and practical effect to the scheme"', and said that "pension scheme documents have to be construed in the light of the requirements of the Inland Revenue Commissioners from time to time for their approval of the scheme". Mr. McDonnell also relied on Warner J.'s observation at p 1611 that

I "the relevant background facts [in that case] or surrounding circumstances included common practice from time to time in the field of pension schemes

generally, as evinced in particular by the evidence of the actuaries and by textbooks written by practitioners in that field". A

36. As Mr. McDonnell accepted, however, the word "retire" is not a term of art, and although it is of course used with great frequency in pension schemes it is to be given its ordinary and natural meaning. It is a matter of fact whether, B in any particular circumstances, someone can be said to have "retired", and the answer will depend upon the context. Whether pensions practitioners generally thought that certain types of transition would amount to retirement, or whether the PSO did or did not think so, has very little bearing on the question actually under appeal. As Mr. Hayward records of the PSO in his evidence, every case has to be considered on its merits. C

37. I must however deal with an argument advanced by Mr. Brennan on the meaning of "director". Because after 1994 Mr. Venables remained a director, albeit a non-executive director, he was, says Mr. Brennan, an employee of the company and, being such, he could not have retired. In support of this argument D Mr. Brennan points to the definition in s 612, to which I have referred, of an "employee" as including a director or any person taking part in the management of the affairs of the company. Since, after 30 June 1994, Mr. Venables was a director, he must therefore have been an employee, and if he was an employee he could not be said to have retired.

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38. Put in such stark terms, the argument can be seen to be fallacious, since it does not follow that because the term "employee" includes someone who is a director, any non-executive director has not retired from whatever he was doing when he was an executive director. An executive director might well retire as such on the grounds of ill health, become a non-executive director so that the board F could from time to time have the benefit of his experience of the business and yet, on Mr. Brennan's argument, be considered not to have retired at all because he is still formally a director. Or a person who had had an executive role as a director, let us say as finance director, might retire from that position but, to ease the transition from an active to an inactive life, he might be made responsible for the running of a small branch of the business, in which case because he would G remain a person taking part in the management of the affairs of the company, he would be deemed not to have retired.

39. A further objection to that line of argument was advanced by Mr. McDonnell and I think that it has much force. It is that under an exempt H approved scheme the maximum amount of the pension and the lump sum which can become payable is limited by reference to the scheme member's final remuneration. That is typically defined by reference to remuneration in the last three years of pensionable activity, or to such a period in the last ten years before retirement. To regard an activity of the kind referred to in the definition of I "employee" in s 612 as necessarily postponing retirement would clearly be apt to distort the calculation of the employee's pension benefits, in some cases very seriously. So to interpret the legislation would produce an anomaly which would discourage early retirement on any but the most absolute and legalistic basis, and would constitute an widening of the tax charge for which the wording of s 600 provides no clear warrant.

A 40. Section 600 does indeed not refer to retirement, but to payments not authorised by the rules of the pension scheme in question. If as a matter of fact, Mr. Venables had retired when he received the payments, the circumstance of his having a continuing interest in the company's affairs as a principal shareholder, in which capacity it was entirely sensible for him to have been a non-executive member of the board, cannot alter the fact of his retirement as an employee and B executive of the company. It is true that the section does charge "any payment to or for the benefit of an employee", but only to those payments made "otherwise than in the course of payment of a pension"—and I take the payments made under clause 5(b) of Sch F in this case to be payments made in the course of payment of a pension. The section must therefore contemplate payments being made to persons within the definition of "employee" which are nonetheless C not chargeable to tax. It is thus not surprising to find that a taxpayer may at the same time have retired for the purpose of an approved pension scheme, have received a payment in the course of his pension under that scheme, but still be within the definition of "employee" in s 612.

41. I conclude therefore that because Mr. Venables was not in normal health on 30 June 1994, he did not so retire within the meaning of clause 2 of Sch D F to the trust deed, and that the payments made to him were therefore not "expressly authorised by the rules of the scheme". If that construction of the effect of Rule 5 and clause 2 is wrong, and the Scheme should be interpreted as permitting the payment of pension benefits on early retirement otherwise than in normal health, I would hold that Mr. Venables did retire for the purposes of the Scheme on 30 June 1994, because he thereafter ceased to be an executive director E or an employee of the company, and had no normal, usual or definite role in its management.

Breach of Trust

F 42. A further plank in Mr. McDonnell's case was the argument that if the payments to Mr. Venables had been made so as to attract tax under s 600, they must have been made in breach of the terms of the trust and, Mr. Venables being one of the trustees, therefore continued to hold the money as such; in which event, he could not be said to have received anything in his personal capacity and the assessment must fail.

G 43. I believe that the point can be dealt with quite shortly by reference to the wording of s 600 itself. Subsection (2) refers, by way of identifying the chargeable event, to any payment "not expressly authorised by the rules of the scheme". If the scheme is an approved scheme, it is true that a lump sum payment made in accordance with its rules would not be expected to be such that, as a matter of the policy of the legislation, it should be within the Sch E charge to tax.

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44. This section accordingly targets payments which might be outwith the rules approved by the Revenue, but says nothing about whether they would have been made in breach of trust. That is because the evident purpose of s 600 is to provide a safety net to the Exchequer where, for one reason or another, and despite previous approval of a scheme, the terms of that approval are not I respected in practice. If they are not, the relief afforded to an approved pension scheme provides no shield to the recipient of the payment. For the purpose of

s 600, it is beside the point that there has, in addition to a breach of the rules of the scheme, been a breach of trust. There may commonly be, but sometimes not: either way, the tax is charged. A

45. Nonetheless, there is some authority to support Mr. McDonnell's thesis. It is *Hillsdown Holdings Plc* v. *Inland Revenue Commissioners* [1999] STC 561, a decision of Arden J. on s 601 of the 1988 Act. The material facts of the case were that Hillsdown acquired a subsidiary company whose pension fund was in surplus, and the trustees of the fund in surplus transferred the assets and liabilities of their fund to Hillsdown's pension scheme. The rules of the subsidiary's pension scheme had prohibited the reduction of a surplus by means of a transfer of assets to the employer, but the rules of Hillsdown's scheme allowed it. After the enhancement of the benefits enjoyed under the first scheme, Hillsdown's scheme was itself in surplus and the surplus was reduced, with Revenue approval: the surplus was then paid to Hillsdown, subject to the payment to the Inland Revenue of tax due under s 601, which charges "payments made to an employer out of funds which are or have been held for the purposes of a scheme". B C D

46. It was held that, *inter alia*, the payment to Hillsdown (by means of the transfer of assets) was in breach of trust and that Hillsdown, as a constructive trustee of the assets holding them for the benefit of the trustees of the scheme, had in law received nothing and that it was not liable accordingly under the section. That view of the position, as a matter of trust law, had resulted from an order by the Pensions Ombudsman to Hillsdown to repay the scheme trustees, an order moreover upheld on appeal by Knox J. in *Hillsdown Holdings Plc* v. *Pensions Ombudsman* [1997] 1 All ER 862. The obligation of Hillsdown to make restitution had been established and was not in dispute. Arden J. said, at p 571 *a* and *h*: E F

> "In my judgment there is no reason in the present case why Parliament should seek in s 601 to tax a payment which was not effectively made, and indeed the policy of the sections would, as [Hillsdown] submitted, suggest otherwise. . . . In my judgment, these words [in s 601(1)] indicate that the payment must result in funds effectively leaving the fund as intended by the transaction (whether absolutely or for a period, as in the case of a loan). The words 'out of' are not apt to describe a payment which, contrary to the stated effect of the transaction, does not have the effect of changing the ownership of the moneys paid **and is in fact reversed**." (my emphasis) G

47. That is not the case here: I have had no evidence that Mr. Venables knew or should have known that the payments to him were in breach of trust; indeed, from what I can deduce it is more than likely that he acted in good faith, on professional advice, and did not once suppose that he was involved in committing a breach of trust. Moreover, no breach of trust has yet been established; it cannot simply be assumed that if there is a charge to income tax, such a breach must inevitably have occurred. H I

48. The needs of this case seem to me to call more for the approach adopted by the Court in *R* v. *Inland Revenue Commissioners* ex parte *Roux Waterside Inn Ltd.* [1997] STC 781—which appears not to have been referred to in *Hillsdown*. In that case, assets of an approved scheme were transferred to a second scheme

A which was seeking, and on the face of it entitled to, Revenue approval. On such a transfer, no charge to tax would in principle arise, but the Revenue withdrew approval from the first scheme when it appeared that the trustees of the second scheme had become non-resident and that the object of the exercise had been to extract a payment from the first scheme without payment of tax in circumstances in which it would otherwise have been chargeable; the effect was to trigger a B charge to tax under s 591C of the 1988 Act.

49. But it was argued, somewhat as here, that the transfer to the second scheme was invalid and that the trustees of the second scheme held the assets on constructive trusts for the trustees of the first scheme: the effect of that would have been to remove the basis for the Revenue's withdrawal of its approval. Of C this argument, Tucker J. said, at [1997] STC 781 pp 787–788:

> "As I understand the law, equity imposes a constructive trust, upon trust or other property subject to a fiduciary relationship, or upon its traceable product where such property has wrongfully been transferred by a fiduciary to a stranger [and text authority is then cited]. If there is any such D doctrine I cannot believe that it can have any application to a situation such as that in the present case, where, in my view, no injustice has occurred and where the imposition of equitable relief is unrequired and inappropriate. The taxpayer entered into these schemes, presumably after taking professional advice, in full knowledge of what was involved and with the sole objective of avoiding payment of tax. He must have known, or must be presumed to have known, of the risks of Revenue disapproval and of all that E that involved, but he must have considered the fiscal advantages sufficiently attractive to warrant the taking of that risk."

50. I make it quite clear that there is no suggestion here of the payments made to Mr. Venables being made as part of a tax avoidance scheme but, apart F from that difference—which I do not think alters the statement of principle involved at all—the learned Judge's observation can be applied well enough to what has occurred and is now the case with the Fussell Pension Scheme, the only important difference between this case and the facts in *Roux* [1997] STC 781 being that there are I believe other beneficiaries in the Fussell Scheme whose interests might have been prejudiced by a wrongful transfer and who might be G entitled to call for restitution to the fund—though even in *Roux's* case there was a further beneficiary involved, and that fact did not alter the conclusion. However that may be, I do not see the constructive trust argument as made out in the circumstances of this case.

Human Rights

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51. The final argument on behalf of the taxpayer was that the PSO's alleged inconsistency of treatment of taxpayers in the same essential position amounted to unlawful discrimination contrary to Article 14 of the European Convention on Human Rights and Fundamental Freedoms, as applied to the circumstances of this case by the Human Rights Act 1998. The argument depends on the I relationship between Article 14, and Article 1 of the First Protocol to the Convention. They provide as follows:—

"Article 14

The enjoyment of the rights and freedoms set forth in this Convention shall be secured without discrimination on any ground such as sex, race, colour, language, religion, political or other opinion, national or social origin, association with a national minority, property, birth or other status.

First Protocol

Article 1

Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law.

The preceding provisions shall not, however, in any way impair the right of a State to enforce such laws as it deems necessary to control the use of property in accordance with the general interest or to secure the payment of taxes or other contributions or penalties."

52. It is said in effect that the kind of lack of fairness in treating taxpayers differently when their circumstances are alike, which the courts will sanction on judicial review, is capable also of being a breach of Article 14 which s 6 of the Human Rights Acts makes unlawful, and which s 7(1)(b) requires me take account of. Indeed, it is said that the Special Commissioners themselves, being a "public authority" within s 6(3), will have committed a breach of Article 14 if the appeals are not allowed because the appeal decision must respect the rights granted by the Convention in the same way as the PSO should have done. The case is decided after 2 October 2000, when the Act came into force, so the possibility suggested by Mr. McDonnell's argument is a real one.

53. But I have indicated above that the evidence which is supposed to show discrimination by the PSO does not in my view do so, or get anywhere near doing so. The best that can be said of it is that it raises a *prima facie* case which might, conceivably, be sufficient to get leave for judicial review. In the circumstances, that is enough in itself to dispose of the Human Rights argument, but I will nonetheless address two further points which arise in connection with it.

54. The first is that s 7(1)(b) of the 1998 Act applies to the case, notwithstanding that the events of which complaint is made took place long before then. That is because s 22(4) of the Act, about commencement, provides:—

"(4) Paragraph (b) of subsection (1) of section 7 applies to proceedings brought by or at the instigation of a public authority whenever the act in question took place; but otherwise that subsection does not apply to an act taking place before the coming into force of that section."

55. In view of the findings of fact I have made it is in a sense academic whether this has the effect of disapplying the Convention, as a matter of domestic law, to the present case. It is doubly academic if Mr. McDonnell is right that any decision repeating or compounding an antecedent breach by a public authority is itself a breach of the Convention, whether or not—as Mr. McDonnell argues—

A the Commissioners have, by virtue of their power under s 50 of the Taxes Management Act 1970 to determine or reduce an assessment, an administrative and a judicial function, or only the latter.

56. I will not therefore go into the arguments in any detail, but I express the view that these appeals are not proceedings brought by or at the instigation of B the Inland Revenue, or the Inspector on their behalf. The mechanism of assessment under s 29 of the Act and the concomitant rights of appeal are well known and it is not necessary to rehearse them here. The decision to initiate these proceedings is that of the taxpayer and of nobody else. Thousands of assessments are issued each year which are not appealed and it would be strange if proceedings had thereby been initiated or brought by the Revenue: nothing is at C that point before any court or tribunal, and in most cases nothing ever will be. If there is to be some doctrine of relation back to the assessment when and if an appeal is made, then one would expect that to be clear from the statute itself.

57. The other point I should deal with relates to the citation of Human Rights decisions. In a brief report in the Times of 24 October 2000 of *Barclays Bank Plc* v. *Ellis & Another* the Court of Appeal is reported as saying:—

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> "If counsel wished to rely on the provisions of the 1998 Act they had a duty to have available any material in terms of decisions of the European Court of Human Rights which they relied on or which would help the court. Mere reference to the Convention did not help the court. Argument needed to be formulated and advanced in a plausible way."

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58. Even if the factual evidence had been much more detailed and wide-ranging than it was, and the issue had been seriously arguable on the facts, I would still have needed considerable assistance in the way of citation of ECtHR decisions before being able to conclude (a) that, in spite of decisions known to suggest the contrary, the Convention is indeed capable of being prayed in aid in tax liability cases, and (b) that Article 14 can be relied upon by a taxpayer either F to claim that an unpublished but withdrawn concession, or a debatable but abandoned practice, should be extended to him and (c) that the matter is not within the margin of appreciation often allowed to the state in such circumstances. No authorities of the ECtHR were cited. It may be that the issue of discrimination can be pursued on judicial review, and that appropriate authority can be cited there, but in the present proceedings the argument on G Article 14 must fail.

Conclusion

59. In view of what has gone before, the assessment and the determination H must be confirmed. It is agreed that there is an arithmetical error in regard to the payments to Mr. Venables referred to in the Regulation 49 determination and that they should total £580,591: the determination is increased accordingly.

Malachy Cornwell-Kelly

Special Commissioner

13 November 2000

I

The taxpayer's appeal was heard in the Chancery Division before Lawrence Collins L.J. on 27 April 2001 when judgment was reserved. On 14 June 2001 judgment was given against the Crown, with costs. A

Conrad McDonnell for the taxpayers.

Timothy Brennan Q.C. for the Crown. B

The cases referred to in the judgment were as follows:—*Harris* v. *Lord Shuttleworth* [1994] ICR 991; *Hillsdown Holdings plc* v. *Commissioners of Inland Revenue* (1999) 71 TC 356; [1999] STC 561; *Investors Compensation Scheme Ltd.* v. *West Bromwich Building Society Ltd.* [1998] 1 WLR 896; *Mettoy Pension Trustees Ltd.* v. *Evans & others* [1990] 1 WLR 1587; [1991] 2 All ER 513; *R* v. *Commissioners of Inland Revenue* ex parte *Roux Waterside Inn Ltd.* (1997) 70 TC 545; [1997] STC 781; *Re Courage Group's Pension Schemes, Ryan & others* v. *Imperial Brewing & Leisure Ltd.* [1987] 1 All ER 528. C

The cases cited in the arguments were as follows:— *Derby Daily Telegraph Ltd.* v. *Pensions Ombudsman & another* [1999] ICR 1057; *Proudfoot plc* v. *Federal Insurance Co.* [1997] LRLR 659. D

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Lawrence Collins J.:—

Introduction F

1. This is an appeal from a decision of Special Commissioner Cornwell-Kelly dated 13 November 2000, which raises the question *(inter alia)* of the meaning of "retirement" for the purposes of entitlement to a pension in the light of the tax legislation. The Revenue claims that pension payments made to Mr. Venables at the age of 53 when he ceased to be an executive director of the company of which he and his family trusts were the controlling shareholders are chargeable to tax under s 600 of the Income and Corporation Taxes Act 1988 ("the 1988 Act"), because he remained a director and therefore did not retire for the purposes of the company's pension Scheme Trust Deed and Rules. His normal retirement age was 60, but the trustees had power to award an immediate pension to a member of the Scheme "who retires in normal health at or after the age of fifty." The Special Commissioner decided that Mr. Venables had retired, notwithstanding his continued connection with the company, but that the assessment should be upheld on the ground that, although he had retired, he had not, in view of the evidence about his medical condition, retired "in normal health." Mr. Venables and the trustees appeal from the second determination, and the Revenue cross-appeals on the first determination. A further issue arises if the Revenue is right on either of those points. Mr. Venables argues that if the payments were made outside the powers of the trustees and so as to attract tax under s 600 of the 1988 Act, then the payments were made in breach of trust to a trustee (Mr. Venables) who therefore continued to hold the money as trustee, G H I

A and therefore he could not be said to have received a "payment." Mr. Venables appeals from the decision of the Special Commissioner that there was a relevant payment chargeable to tax.

The facts

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2. Mr. Venables was born on 14 December 1940. He is a substantial shareholder in Ven Holdings Ltd. ("the company"), having in his own right 20 per cent. of the shares and, as settlor and a trustee of his family discretionary trust, the remaining 80 per cent. The company has a number of subsidiaries and the main business of the group is property development. At the relevant time in 1994 the group consisted of eight companies with assets of some £4 m.

C

3. Mr. Venables worked in the business for more than 30 years, and had for some time been an executive director and the chairman of the company, in which capacity he worked about 30 hours a week. On 31 March 1993, the group's managing director retired, and Mr. Venables' workload increased so that he then worked nearly 50 hours a week. Before that, he had been occupied for the most D part in making strategic decisions concerning the activities of the group, but from March 1993 he became responsible for its day to day running, arranging the finances, costing work and recruiting staff.

4. Mr. Venables was anxious to give more of the responsibility to his children Steven and Paula, and a man called Luke Singleton. By 1994 he had E decided to cease to undertake all the responsibilities that he had had since March 1993: Mr. Singleton became managing director (which post he continued to fill until 1998, when Steven Venables took over); Paula Venables became company secretary on 23 June 1994.

5. On 23 June 1994 the board minutes recorded that Mr. Venables was "retiring as an executive director on 30 June 1994 to pursue other interests but F will continue as an unpaid non-executive director." The Special Commissioner found that "concern about his health was part of Mr. Venables' reason for wanting to pass on his newly acquired responsibilities after so short a time and when he was only 53."

6. On 23 June, Mr. Venables wrote to his pension consultant to say that G although he had decided to retire from employment with the group from 30 June he hoped to be involved in one or two new business ventures outside the property companies, and that he wanted to take most of his lump sum from the Scheme in the form of property.

7. Thereafter, the Special Commissioner found:

H

> ". . . Mr. Venables spent a large proportion of his time in North America, buying a house in Florida in May 1996, though from time to time returning to the UK. In spite of the distance in time and place, Mr. Venables nonetheless continued to be interested in the running of the company, since he remained—either on his own account or as a trustee—the major shareholder. He tried to guide the family in what they were doing: they could I telephone him to seek advice on a wide range of matters—how they should deal with the bank manager? what rates should they pay? how best to twist

his arm? would this or that building be likely to be a good acquisition? Mr. Venables had a store of experience and business sense on which his family were glad to draw. A

It was all usually done by telephone, and Mr. Venables received no remuneration from the company to recompense him for his interest in its fortunes. As a trustee of the family trust, and as the originator and hitherto the mainstay of the business, it was natural for him to take that interest, and as trustee he was actively involved in the trust's investment deals. He might tip the company off about a good deal, or even on occasion cut a bargain on his own account, because he owned a small property company of his own. It was in his blood, and he did not lose interest in his lifetime's work in a single moment. B C

But Mr. Venables no longer went to the sites as he had done before June 1994, or normally attended at the office. As a non-executive director, and still ultimately in control through shareholdings, Mr. Venables was useful, conscientious and available, even addressing himself to particular matters such as the adequacy of credit control; he did not, however, run the company and could in his personal circumstances scarcely have done so ... his health was not good, and during the period we are concerned with he had three heart attacks, and he was for the most part physically absent—not an hour's drive from the business, but on the other side of the Atlantic. It was shown that on one occasion after June 1994 he had signed off the company's accounts, but he didn't normally do so." D E

8. Mr. Venables remained as a director of the company at all relevant times during 1994–95 and continued as a director after 5 April 1995. But after 30 June 1994 he became an unpaid non-executive director, and ceased to be an employee. F

9. The Scheme paid Mr. Venables £580,591 in three tranches between July and August 1994. On 5 March 1997 Mr. Venables was assessed to tax under Sch E for the year 1994–95. On 21 March 1997 Mr. Venables appealed against this assessment. On 1 March 1999, pursuant to Regulation 49 of the Income Tax (Employments) Regulations 1993, a determination was raised upon Mr. Venables and Denton & Co. Trustees Ltd., as trustees of the Scheme. G

The Pension Scheme

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10. The Scheme was established on 25 September 1980 by a Trust Deed made between Fussell Estates Ltd., Mr. Venables and Neill Alexander Denton, to provide relevant benefits for directors and employees of Fussell Estates Ltd. On 26 May 1989 the terms of the Trust Deed were amended so that thereafter Ven Holdings Ltd. was treated as the Founder of the Scheme in place of Fussell Estates Ltd. With effect from that date the participating employers under the Scheme were (1) Ven Holdings Ltd. and (2) Fussell Management Ltd. With effect from 1 April 1993 the trustees of the Scheme were (1) Mr. Venables and (2) Denton & Co. Trustees Ltd. It was an "approved" Scheme for the purposes of the Finance Act 1970, but it ceased to be approved on 5 August 1994, after the payments in question in this case, because it did not amend its Rules to comply I

A with the Retirement Benefits Schemes (Restriction on Discretion to Approve) (Small Self Administered Schemes) Regulations 1991.

11. The Trust Deed recited (Recital A) that the Scheme was being established to provide relevant benefits as defined in s 26(1) of the Finance Act 1970, and clause 1 established the Scheme "under the provisions of this Deed and B the Rules made hereunder". By Sch A, para (2) "each Member's Rules shall complement the Trust Deed and both shall be construed together," and the list of defined terms included "Employee," which was defined to mean a person in the service of the Employer and including a director, and "Service", which meant service with an employer for the purposes of the Trust Deed and the Rules. The normal retirement date was to be in the range 60 to 70. The Rules are defined in C Sch A by reference to clause 2 of Sch D, which provides:—

> "2. Upon an Employee being offered membership of the Scheme a letter with an appendix attached setting out the terms conditions contributions to be made by the Employer and the Employee respectively and benefits to be provided will be drawn up in a form acceptable to the D Commissioners of Inland Revenue and signed so as to indicate acceptance by the Employee and by an authorised signatory of the Employer. Upon acceptance the said letter with the appendix attached will be the Rules applicable to such member and may be superseded in whole or in part by subsequent letters duly signed and accepted in the manner stated above. The Rules with this Deed will be binding (although the Rules be not under seal) on the Member the Employers and the Trustees"

E

12. Clause 2 of Sch B to the Trust Deed provides that:

> "Subject to the powers to be exercised by the Employers as herein expressed the Trustees shall have full power to determine in consultation with the Founder whether or not any person is entitled from time to time to F any benefit or payment in accordance with the Scheme and in deciding any question of fact that they shall be at liberty to act upon such evidence or presumption as they shall in their discretion think sufficient although the same be not legal evidence or legal presumption. Subject as aforesaid the trustees shall also have power to determine all questions and matters of doubt arising on or in connection with the Scheme and whether relating to G the construction thereof or the benefits thereunder or otherwise."

13. By Sch F:

> "**Normal retirement**
>
> 1. . . . on retirement at the Normal Retirement Date a Member shall be H entitled to receive such benefits as are stated in the Member's Rules
>
> **Early retirement**
>
> 2. With the consent of the founder the Trustees have discretion to award an immediate pension to a Member who retires in normal health at or after age 50. The amount of pension will be calculated as for deferred pensions . . . I and will then be reduced by such a proportion as the Actuary determines having regard to the Member's age at retirement . . . As an alternative to an

immediate pension the retiring Member may elect to receive a deferred pension payable from his Normal Retirement Date . . ." A

and by clause 5(b) provision was made for commutation of pension for a lump sum.

14. The Scheme Rules applicable to Mr. Venables, and communicated to him at the same time as the Trust Deed was executed, include the following:— B

"2 You will normally retire from the Company's service on 13 December, 2000, your Normal Retirement Date, when you will be aged 60 years and you will have been a member of the Company for more than 20 years. . . . You may elect to take part of your Capital Sum in the form of a tax free cash sum of up to a maximum of 150% of your Final Remuneration as defined in the Trust Deed. . . . C

5 The following paragraphs describe the general conditions relating to the payment of your benefits. However, it is the Trust Deed which governs these conditions and it will always take precedence over this Rule.

D

(a) Retirement before Normal Retirement Date

With the Company's consent you may retire at any time after age 50. At the date of actual retirement, your Capital Sum in the Scheme would be realised to provide reduced benefits . . ."

E

The retirement issue

15. The Special Commissioner found that until 30 June 1994 Mr. Venables had acted as managing director without having been formally appointed as such and that he performed the functions which would have been performed by a managing director if there had been one. After that date he was an unpaid non-executive director, and ceased to be an employee. The conclusion, on the basis of the facts stated above in para 7, was that Mr. Venables did not retire from the office of managing director, because he had never been appointed to it, but he did retire from employment with the company and normal service on its behalf. He retired for the purposes of the Scheme on 30 June 1994, because he thereafter ceased to be an executive director or an employee of the company, and had no normal, usual or definite role in its management. F G

16. The Revenue's position on this appeal is as follows: (a) the Rules and the Trust Deed must be construed by reference to the prevailing tax legislation; (b) retirement, both in ordinary parlance and under s 612 of the 1988 Act, connotes vacation of an office or employment, and directorship is equated to employment; (c) Mr. Venables' only relevant office or relationship was that of director, and he held that office at all material times, and there was therefore no vacation of any office, and no termination of a relationship; (d) there was no evidence of a contract of employment, and no finding that there was any resignation or termination of the contract; (e) the reduction of work-load is all that happened, and that does not amount to retirement. H I

17. Mr. Venables' position is: (a) the provisions of a Trust Deed should wherever possible be construed to give reasonable and practical effect to the

A Scheme, and the relevant background facts or surrounding circumstances (in the light of which they should be construed) include the requirements of the Revenue for approval of a Scheme, and common practice in the field of pension schemes generally; (b) retirement means withdrawal from some activity or position, and in the pension context it is the cessation of active, pensionable service; (c) an executive director may retire from employment and the office of director at B different times, but it is the retirement from remunerated employment which is crucial, and there is no practical or purposive reason why cessation of office as a non-executive director should be the relevant event triggering payment; (d) if the Revenue were right, there would be a risk that "final remuneration" would be reduced by the effect of including a period as an unpaid non-executive director; (e) the statutory definition in s 612 of the 1988 Act is of no assistance, and the C Trust Deed and Rules make no reference to it; (f) Recital A of the Trust Deed applies to benefits in anticipation of retirement or in anticipation of or in connection with any change in the nature or service of the employee in question, and an exempt approved Scheme may lawfully provide a pension (including a lump sum) on early retirement, notwithstanding that it does not fall within the statutory definition of "retirement."

D 18. The Scheme in the present case was approved by the Revenue under the Finance Act 1970. Like the 1988 Act, the 1970 Act required the Revenue to approve a Scheme which complied with the statutory conditions, including the condition that it provided benefits on retirement at an age not earlier than 60 or later than 70 (1970 Act, s 19 and Sch 5, para 1 and 1988 Act, s 590(3)(a)), but gave the Revenue the discretion to approve Schemes which did not satisfy the E prescribed conditions, including those making provision for early retirement: see now 1988 Act, s 591(2)(d).

19. The legislation (1988 Act, s 612(1), re-enacting 1970 Act, s 26(1)) defines (a) "employee" in relation to a company to include any director, and (b) "service" to mean "service as an employee of the employer in question and other F expressions, including 'retirement,' shall be construed accordingly."

20. Section 600 of the 1988 Act, as amended, applies to

> "any payment to or for the benefit of an employee, otherwise than in course of payment of a pension, being a payment made out of funds which are held for the purposes of a scheme which is approved for the G purposes of [the 1970 Act and the 1988 Act]," (s 600(1)), and

s 600(2) provides:

> "If the payment is not expressly authorised by the rules of the scheme . . . the employee . . . shall be chargeable to tax on the amount of the payment under Schedule E for the year of assessment in which H the payment is made."

21. Consequently the question for the purposes of s 600(2) is whether the payment is expressly authorised by the Rules of the Scheme.

22. As is clear from the provisions of the Trust Deed and the Rules set out I above, there is an inconsistency between the Trust Deed and the Rules. The Rules provide that with the company's consent, Mr. Venables may retire at any time

after age 50, whereupon his capital sum in the Scheme would be realised to provide reduced benefits. But the Rules are expressly subject to the Trust Deed, which provides that with the consent of the company the trustees have discretion to award an immediate pension to a member who retires in normal health at or after 50. This discrepancy raises the issue which is dealt with in the next section of this judgment.

23. It is clear from s 600(2) that the question is whether the payment is authorised by the Rules, and not whether it is authorised by the legislation or, still less, by the Revenue. Accordingly the question is one of construction of the Rules of the Scheme. In *Re Courage Group's Pension Schemes* [1987] 1 WLR 495, at p 505 Millett J. said:

> ". . . there are no special rules of construction applicable to a pension scheme; nevertheless, its provisions should wherever possible be construed to give reasonable and practical effect to the scheme, bearing in mind that it has to be operated against a constantly changing commercial background."

24. That statement was approved by Warner J. in *Mettoy Pension Trustees Ltd.* v. *Evans* [1990] 1 WLR 1587, at pp 1610–1611, who added that, although there were no special rules governing the construction of pension Scheme documents

> "... the background facts or surrounding circumstances in the light of which those documents have to be construed—their 'matrix of fact' to use the modern phrase coined by Lord Wilberforce—include . . . special factors. The first factor is that . . . the beneficiaries under a pension scheme such as this are not volunteers. Their rights have contractual and commercial origins. They are derived from the contracts of employment of the members. The benefits provided under the scheme have been earned by the service of the members under those contracts and, where the scheme is contributory, pro tanto by their contributions. Secondly, as was common ground, pension scheme documents have to be construed in the light of the requirements of the Inland Revenue Commissioners from time to time for their approval of a scheme . . . Thirdly it was also common ground that the relevant background facts or surrounding circumstances included common practice from time to time in the field of pension schemes generally, as evinced in particular by the evidence of the actuaries and by textbooks written by practitioners in that field."

25. In the present case there was some evidence before the Special Commissioner from a former official at the Superannuation Funds Office of the Revenue, the predecessor of the Pension Schemes Office, to the effect that it was between 1979 and 1988 the practice to agree the mode of early retirement in individual cases, and in particular to approve pension payments for directors who changed from an executive role to a non-executive role, and that the practice had become so established that where a director became a non-executive director after age 50, early retirement benefits were often taken without an approach being made to the Revenue beforehand. The Special Commissioner decided that the evidence was too sketchy and speculative to be of assistance, and in particular was not apt to assist in the construction of the Trust Deed. It was not argued on this appeal that the Special Commissioner was wrong in this conclusion, although Mr. McDonnell drew my attention to a recent Revenue manual which

A suggests that there is no incompatibility between retirement and the retention of a directorship with the former employer. But if Warner J. was right (as I think he was, although it seems that Glidewell L.J. in *Harris* v. *Lord Shuttleworth* [1994] ICR 991, at p 1003, had some doubts about the admissibility of Revenue practice as an aid to construction) in saying that among the relevant surrounding circumstances for the purpose of construction of the Rules (as distinct from the B legislation) is the then prevailing Revenue practice, it is regrettable that evidence of the practice as known to pension practitioners at the time when Mr. Venables became a member of the Scheme in 1980 was not available.

26. Since the Trust Deed and Rules were drafted against the background of the legislation and the need to obtain Revenue approval, they must be construed C against the background of the legislation. But I do not derive any assistance from the references in the legislation to "employee," "service," and "retirement." It is true that employee includes a director, and that therefore service includes service as a director. But the provision that "other expressions, including 'retirement,' shall be construed accordingly" (s 612(1)) does not, in my judgment, help to determine whether, for the purposes of the Trust Deed and the Rules, a paid executive director who ceases to be such, and becomes an unpaid non-executive D director, is a person who "retires" within the meaning of the Trust Deed or the Rules. More relevant in the present case is that the Trust Deed (Recital A) states the purpose of "providing relevant benefits as defined in s 26(1) of the Finance Act 1970" for directors and employees. "Relevant benefits" in s 26(1) (and in the 1988 Act, ss 612(1)) means any pension

E "given or to be given on retirement or on death, or in anticipation of retirement, . . . or to be given on or in anticipation of or in connection with any change in the nature of the service of the employee in question."

While this does not assist in the meaning of the expression "retirement" it clearly shows that a change in the nature of the service of an employee can qualify the employee to benefits, and that an exempt approved scheme may lawfully F provide a pension on early retirement in such circumstances.

27. In my judgment the Trust Deed and the Rules have to be given a practical and purposive construction. In *Harris* v. *Lord Shuttleworth* [1994] ICR 991, at p 1001, the Court of Appeal was concerned with the question whether an employee who had been dismissed for substantial absences for sickness had left G on "retirement . . . by reason of incapacity." It decided that the employee had retired as a result of incapacity. It emphasised that the right to a pension is delayed remuneration for which the employee has given consideration, and that

"the rules which provide for the payment of pensions on early retirement, whether that comes about at the wish of the employee or on the direction of the employer, in each case within a few years of normal pension age, are but H variants on the normal theme" (at p 1005).

That case is not directly relevant, but it does show that the Rules must be interpreted in a common sense and commercial manner.

28. There is no clear distinction in law between an executive and non-I executive director. But I do not consider that there can be a principle that, in Rules in form similar to those in this case, a person who is a director, and who

has executive responsibilities and is paid, whether or not he or she has a designated office such as managing director, and who subsequently ceases to be paid and have executive responsibilities, does not "retire." If there were such a principle it would have odd and uncommercial consequences, particularly with regard to the calculation of final remuneration. In my judgment it is a matter of fact and degree as to whether a person has retired, which in my view connotes withdrawing from active work. I accept the contention by Mr. Brennan Q.C. for the Revenue that a mere reduction in workload is not retirement, but I do not accept the contention that the only relationship Mr. Venables had with the company was that of director, and that because he never ceased to be a director he never retired. In this case there was substantial evidence on which the Special Commissioner came to his conclusion that Mr. Venables had retired. He was previously working in effect as managing director for 50 hours a week. There was evidence that he was anxious to give up work because of concerns about his health. There was some direct evidence that he had been remunerated, and substantial indirect evidence from the size of the pension payments. His activities thereafter could be regarded as those of an interested and knowledgeable shareholder who had built up the business, who (with his family trusts) was a controlling shareholder, and who was keen to preserve the value of the holding, and whose advice was respected by those who carried on the business. There was sufficient evidence for the Special Commissioner's decisions on the facts, and in these circumstances there are no grounds for interfering with it.

The "normal health" issue

29. Although the evidence was not altogether clear, for present purposes the position can be taken to be as follows. At the time of his retirement Mr. Venables was seriously overweight (21 stone), and his blood pressure was high. He was mildly diabetic. The Special Commissioner found that concern about his health was part of Mr. Venables' reason for wanting to pass on his newly acquired responsibilities after so short a time, and when he was only 53. Mr. Venables suffered three heart attacks, but the Special Commissioner accepted that those attacks, and the more serious diabetes which he developed and for which he took medication from 1995, all occurred after 30 June 1994.

30. There are two oddities about the Rules and the Trust Deed. First, the Rules permit retirement at any time after the age of 50 with company's consent, but the Trust Deed refers only to a member "who retires in normal health at or after the age of fifty," and the Rules expressly provide that the Trust Deed is to take precedence over the relevant Rule. Second, neither the Rules nor the Trust Deed contain any provision for retirement on the grounds of ill health or incapacity. The consequence, if the Special Commissioner and the Revenue were right, would be the bizarre and uncommercial one that the more ill and the more disabled an employee aged over 50 were, the less able he or she would be to retire early.

31. The Special Commissioner found that Mr. Venables was not "in normal health" on 30 June, based on the facts stated above. The Revenue relies in particular on the fact that concern about his health was one of the reasons for the resignation, and an important factor leading to his decision to resign.

A Accordingly, the Revenue contends, the Special Commissioner was entitled to come to the conclusion that he did not retire in normal health.

32. Mr. Venables has several answers to the decision of the Special Commissioner on this point, which, according to Mr. McDonnell, for Mr. Venables, was a point taken for the first time in the decision, and did not form B part of the Revenue's case. I see considerable force in the contention that the reference to "in normal health" is simply surplusage or a drafting error, intended to contrast retirement of a member in normal health after the age of 50 with earlier retirement of incapacity or ill health, and that because no provision for ill health was in fact made by the Rules or the Trust Deed (except in relation to commutation of pension), the reference to normal health can be ignored, on the C basis that "something must have gone wrong with the language": *Investors Compensation Scheme* v. *West Bromwich Building Society Ltd.* [1998] 1 WLR 896, at p 913. I would have so held if there were not a more compelling reason for finding that the Special Commissioner's finding can be interfered with. In my judgment, the Special Commissioner could not reasonably have arrived at the conclusion that, for the relevant purpose, Mr. Venables was not in normal health.

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33. This is so for two reasons. First, even if the Rules and the Trust Deed contain no provision for retirement for ill-health and incapacity, I consider that the expression "in normal health" in the context of a pension scheme Trust Deed cannot be interpreted in a vacuum. "In normal health" must mean "normal" by reference to some standard, and the only standard which can reasonably be E applied is fitness to do the job. Not only was Mr. Venables spending 50 hours a week as an executive director at the time of his resignation, which suggests strongly that he was fit to do the job, but there was no evidence to suggest that he was unfit to do it. Second, there was no evidence to support the finding that even in the abstract Mr. Venables was not in normal health. High blood pressure and mild diabetes are common conditions in overweight middle-aged men, and F there was no finding that his health was abnormal.

34. For the sake of completeness I mention that I would have rejected Mr. McDonnell's three other arguments on this issue. The first was a very strained interpretation of clause 2 of Sch F, which depended on inserting a comma so that it would read "the Trustees have discretion to award an immediate pension to a Member who retires, in normal health at or after age 50" with the consequence G (it was said) that it has the following meaning: the trustees have discretion to award an immediate pension to a member who retires, but if he is in normal health then only at or after age 50, whereas a member who retires other than in normal health can draw an immediate pension with no age restriction. This construction comes close to rewriting the Trust Deed to cure the omission of the provisions for ill-health and incapacity. The second argument was that clause 2 H of Sch B to the Trust Deed confers on the trustees a wide power to determine matters of doubt. But no such question or matter was put to the trustees and they have never purported to do more than make the payment to a person they considered was retiring. Finally, it is suggested that as a deferred pensioner (i.e. a person who had left employment with service benefits but was not yet entitled to a pension), Mr. Venables could have applied for his pension to be commuted I and a lump sum paid to him. But (a) the right to commute a deferred pension for a lump sum arose only when the pension was payable; (b) even if that were wrong

Mr. Venables had never made such an application and the trustees had not exercised their discretion under that power; and (c) there was no evidence as to what lump sum might have been payable.

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The "payment" issue

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35. This issue does not arise in view of my decision on the first two issues, but it was fully argued. The point arises in this way. The effect of s 600(1) and (2) of the 1988 Act is that if a "payment" is made out of funds of an approved pension scheme and "the payment is not expressly authorised by the rules of the scheme" the employee is chargeable to tax. For Mr. Venables, Mr. McDonnell argued that in the circumstances of this case there was no relevant "payment" to him: (a) if the payment to Mr. Venables was not authorised by the Trust Deed or the Rules, then he was not beneficially entitled to it; (b) Mr. Venables was a trustee of the Scheme, and if he was not beneficially entitled to the payment, he could not have taken it free from the trusts of the Scheme; (c) consequently, the money remained subject to the trusts of the Scheme, and nothing accrued to Mr. Venables; (d) accordingly he received nothing and there was therefore no payment to him. The Revenue's position, put by Mr. Brennan Q.C., is that the whole purpose of the section is to impose a charge to tax when money is paid out of pension funds otherwise than in accordance with the Scheme and the Rules, and "payment" should be construed in its ordinary sense, in which event there can, it says, be no doubt that payments were made to Mr. Venables. The Special Commissioner decided Mr. Venables had not shown that the payments were in breach of trust, and that he held the funds as constructive trustee, and that accordingly the point did not arise.

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36. Mr. Venables relied on *Hillsdown Holdings plc* v. *Inland Revenue Commissioners* (1999) 71 TC 356; [1999] STC 561. That was a case on s 601(1) and (2) of the 1988 Act, the effect of which is that, subject to important exceptions, where a payment is made to an employer out of an exempt approved Scheme, an amount equal to 40 per cent. of the payment is chargeable to tax. Such a payment was made by the trustees of the pension fund of FMC Ltd. to the trustees of the pension fund of Hillsdown plc (FMC Ltd.'s parent), and tax was paid, but the pension ombudsman decided that the payment of the surplus assets of the Scheme to the Hillsdown Scheme was in breach of trust and invalid. His decision was upheld, and Hillsdown plc and its pension fund trustees sought to recover the tax which had been paid pursuant to s 601. Arden J. held that the tax was recoverable because (a) the payment in the events which had occurred had not been effectively made; (b) it did not have the effect of changing the ownership of the funds and was in fact reversed; (c) the employer had merely received the money as a trustee for the fund under a trust arising under operation of law. In *R.* v. *Inland Revenue Commissioners*, ex parte *Roux Waterside Inn Ltd.* (1997) 70 TC 545; [1997] STC 781 there was a transfer from one Scheme to another, and the Revenue withdrew approval from the former Scheme because it took the view that the transfer was intended as a device to avoid the restrictions imposed by the Revenue as a condition of approval. The Revenue made an assessment to tax under s 591C of the 1988 Act, which provides that income tax is payable on the assets of a Scheme where approval ceases to have effect. It was argued that approval should not have been withdrawn, because if the transfer of assets to the new Scheme had not been permissible, the transferred assets would

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A have been held by the trustees of the new Scheme as constructive trustees of the old Scheme. Tucker J. held that this was not a case in which equity would have imposed a constructive trust, since it was not a case in which property had been wrongfully transferred to a third party.

37. In this case, if Mr. Venables, who was not only a member of the Scheme, B but also a trustee, had known, or should have known, that the payment was unauthorised by the terms of the trust, then he would have been accountable as a trustee. In such circumstances, the funds would have been recoverable by the trustees, and if they had been recovered, there would have been no effective payment to Mr. Venables. I am of the view that if each and every one of the following conditions is fulfilled, then there is no taxable payment for the C purposes of s 600: that the payment is in breach of trust, that the recipient is accountable to the trustees as an actual or constructive trustee, and that the recipient is able and prepared to account to the trustees. In those circumstances, I would accept that the rationale of the *Hillsdown* (1999) 71 TC 356; [1999] STC 561 case applies, and I would follow it.

D 38. I will therefore allow the appeal, on the basis that the Special Commissioner was right to decide that Mr. Venables had retired, but wrong to decide that the state of his health disentitled him to early retirement benefits.

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The taxpayer's appeal was heard in the Court of Appeal before Peter Gibson, Potter and Chadwick L.JJ. on 5 July 2002 when judgment was reserved. On 18 September 2002 judgment was given in favour of the Crown, with costs.

Conrad McDonnell for the taxpayers.

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Timothy Brennan Q.C. for the Crown.

The cases referred to in the judgment are as follows:—*Hillsdown Holdings plc and another* v. *Commissioners of Inland Revenue* (1999) 71 TC 356; [1999] STC 561, *Mettoy Pension Trustees Ltd.* v. *Evans & others* [1990] 1 WLR 1587; [1991] 2 All ER 513.

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The cases cited in the arguments, in addition to those referred to in the judgment, were as follows:—*Cooke (HMIT)* v. *Blacklaws* [1985] STC 1; *Derby Daily Telegraph Ltd.* v. *Pensions Ombudsman & another* [1999] ICR 1057; *DTE Financial Services Ltd.* v. *Wilson (HMIT)* (2001) 74 TC 14; [2001] STC 777; *Edwards* v. *Bairstow* [1956] AC 14; (1955) 36 TC 207; *Folami* v. *Nigerline (UK)* H *Ltd.* [1978] ICR 277; *Harris* v. *Lord Shuttleworth & others* [1994] ICR 991; *Hoover Ltd.* v. *Hetherington* [2002] EWHC 1052; *MacNiven (HMIT)* v. *Westmoreland Investments Ltd.* (2001) 73 TC 1; [2001] 2 WLR 337; [2001] 1 All ER 865; [2001] STC 237; *O'Kelly* v. *Trusthouse Forte plc* [1984] QB 90; *Parry* v. *Cleaver* [1970] AC 1; *Proudfoot plc* v. *Federal Insurance Co.* [1997] LRLR 659; *R* v. *Inland Revenue Commissioners* ex parte *Roux Waterside Inn Ltd.* (1997) 70 I TC 545; [1997] STC 781; *Re Courage Group's Pension Schemes, Ryan & others* v. *Imperial Brewing & Leisure Ltd.* [1987] 1 All ER 528; *Rose* v. *Humbles (HMIT)*

(1971) 48 TC 103; [1972] 1 WLR 33; [1972] 1 All ER 314; *Sidey* v. *Phillips (HMIT)* (1986) 59 TC 458; [1987] STC 87; *Taupo Totara Timber Co. Ltd.* v. *Rowe* [1978] AC 537; *Yuill* v. *Wilson (HMIT)* (1980) 52 TC 674; [1980] 1 WLR 910; [1980] 3 All ER 7; [1980] STC 460. A

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Chadwick L.J.:—

1. This is an appeal from an order made on 14 June 2001 by Lawrence Collins J. allowing appeals under s 56A(1) of the Taxes Management Act 1970 by the taxpayers, Mr. David John Venables and the trustees of the Fussell Pension Scheme, against the decision of the Special Commissioners given on 13 November 2000. The Commissioner (Mr. Malachy Cornwell-Kelly, sitting alone) had upheld an assessment on Mr. Venables to income tax under Sch E made on 5 March 1997. The assessment was made under s 600 of the Income and Corporation Taxes Act 1988 in respect of three payments made to Mr. Venables in the year of assessment 1994–95 out of funds held for the purposes of the pension scheme. The Commissioner upheld, also, a related determination of tax payable made against the trustees of the scheme under Regulation 49 of the Income Tax (Employments) Regulations 1993 (SI 1993/744) on 1 March 1999. It has been common ground that the assessment and the determination stand or fall together. C D E

2. Section 600 of the 1988 Act, as amended by the Finance Act 1989, is in these terms, so far as material:

> "(1) This section applies to any payment to or for the benefit of an employee, otherwise than in course of payment of a pension, being a payment made out of funds which are held for the purposes of a scheme which is approved for the purposes of . . . (b) Chapter II of Part II of the Finance Act 1970; . . . F
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> (2) If the payment is not expressly authorised by the rules of the scheme . . . the employee . . . shall be chargeable to tax on the amount of the payment under Schedule E for the year of assessment in which the payment is made." G

In that context "employee", in relation to a company, includes "any officer of the company, any director of the company and any other person taking part in the management of the affairs of the company"—see s 612(1) of the 1988 Act. H

3. It is not in dispute (i) that payments of funds held for the purposes of the Fussell Pension Scheme were made to Mr. Venables in July and August 1994, or (ii) that, at the time when the payments were made, Mr. Venables was a director of Ven Holdings Ltd., one of the participating employers under the scheme. The principal issue raised by the appeal is whether the payments were "expressly authorised by the rules of the scheme". A secondary issue is whether, if not authorised by the scheme, the payments—which, it is said, were (on that hypothesis) held by Mr. Venables on trust from the moment that he received them—should be treated for tax purposes as if they had not been made. It is common ground that, if the payments were not authorised, it must follow that I

A (unless they are to be treated as not having been made or, at least, not having been made "out of" scheme funds), Mr. Venables was chargeable to tax on the amount of the payments under the provisions of s 600 of the 1988 Act and a determination under Regulation 49 of the 1993 Regulations was properly made against the trustees in respect of basic rate tax deductible from those payments.

B 4. The Fussell Pension Scheme was established by a trust deed dated 25 September 1980. Its purpose was described in the deed as the provision of "relevant benefits as defined in Section 26(1) of the Finance Act 1970" for directors and employees of the companies who were to be or become participating employers. The benefits payable under the scheme are set out in sch F to the deed. Paragraph 2 in sch F provides that:

C "With the consent of the Founder the Trustees have discretion to award an immediate pension to a Member who retires in normal health at or after age 50. . . ."

It was in the exercise, or purported exercise of that power that payments D totalling £580,591 were made to Mr. Venables out of the funds subject to the scheme.

The underlying facts

5. The underlying facts are conveniently set out in the following paragraphs E of a statement of agreed facts put before the Special Commissioner:

"8. On 26 May 1989 the terms of the Trust Deed were amended so that thereafter Ven Holdings Ltd. was treated as the Founder of the Scheme in place of Fussell Estates Ltd. With effect from that date the participating employers under the Scheme were (1) Ven Holdings Ltd. ('the Company') F and (2) Fussell Management Ltd. With effect from 1 April 1993 the trustees of the Scheme were (1) David John Venables and (2) Denton & Co. Trustees Ltd.

9. At all material times Mr. Venables held approximately 20 per cent. of the shares in the Company. The Family Discretionary Trust, of which Mr. Venables was settlor and a trustee, held the remaining 80 per cent. of G the shares in the Company.

10. On 23 June 1994 a Board meeting of the Company took place at which it was resolved:

'that D J Venables will be retiring as an executive director on 30th June 1994 to pursue other interests but will continue as an unpaid non-executive director. L G Singleton is to be elected to serve as managing H Director for a trial period of six months with Miss P J Venables appointed as Company Secretary.'

11. In a letter of 23 June 1994 to Denton & Co. Mr. Venables said that he would be retiring from service as managing director of the Company on 30 June 1994.

I 12. Mr. Venables remained as a director of the Company at all relevant times during 1994–95 and continued as a director after 5 April 1995.

13. The Scheme paid to Mr. Venables £580,591 as follows:—

7 July 1994	£225,000
18 July 1994	£250,000
4 August 1994	£105,591"

6. I should add (a) that, as at 30 June 1994, Mr. Venables was 53 years of age and (b) that, as the Special Commissioner found, Mr. Venables had not, himself, ever been appointed as managing director of the company. The position is described by the Special Commissioner in para 4 of his decision:

> "Mr. Venables was a carpenter by trade and in the early days had worked on the sites, though he has not done so for many years. Overall, Mr. Venables worked in Ven Holdings for upwards of thirty years, and had for some time been an executive director and the chairman of the company, in which capacity he worked about 30 hours a week. On 31 March 1993, the group's managing director retired and Mr. Venables's workload increased so that he then worked nearly 50 hours a week. Before that, he had been occupied for the most part in making strategic decisions for the activities of the group, but now he became responsible for its day to day running, arranging the finances, costing work and recruiting staff."

The principal issue: were the payments authorised?

7. The principal issue turns on the meaning to be given to the word "retires" in that paragraph. The question before the Special Commissioner was whether Mr. Venables had "retired in normal health" for the purposes of the scheme when, on 30 June 1994, he ceased to have an executive role in Ven Holdings Ltd.; notwithstanding that he continued thereafter to be a director of that company. The Special Commissioner held that Mr. Venables did retire on 30 June 1994; but that, because he was not then in normal health, the power to pay an immediate pension under para 2 in sch F was not exercisable. It is a curious feature of the scheme—although nothing now turns on it—that the power to pay a pension on early retirement, conferred by para 2 of sch F, is not exercisable unless the member is in normal health on retirement; rather than, as might be expected, being exercisable if the member retires by reason of ill-health.

8. The Judge agreed with the conclusion that Mr. Venables had retired—or, at the least, accepted that it was a conclusion of fact which the Special Commissioner had been entitled to reach—but reversed his finding that Mr. Venables was not then in normal health. He thought that that was a finding which could not reasonably be made on the evidence. The Revenue have not sought to challenge the Judge's conclusion on that point. The only question for this Court, in relation to the principal issue, is whether Mr. Venables "retired" on 30 June 1994.

9. Although treated by the Judge as "a matter of fact and degree", it seems to me that the question whether or not Mr. Venables "retired" on 30 June 1994 turns on a short point of construction: does a member of the scheme who is a director of an employer company with an executive role "retire" for the purposes of para 2 of sch F when he gives up his executive role but continues in office as

A a director? In order to explain why I take that view it is necessary to describe the relevant provisions of the scheme and to set them in the context of the legislation which provided the tax benefits which the scheme was intended to enjoy.

The legislative setting

B

10. It is not in dispute that those who established the scheme under the trust deed of 25 September 1980 must be taken to have intended that it would be approved by the Inland Revenue for the purposes of Chapter II in Part II of the Finance Act 1970. If confirmation of that be needed it can be found in para 2 of sch F itself, which limits the amount of pension which can be paid under the power which it confers to an amount "in no case greater than an amount which C would prejudice the Scheme as an exempt approved scheme under Chapter II of Part II of [the 1970 Act]." The reason is obvious: an exempt approved scheme then enjoyed exemption from income tax on income derived from investments or deposits—see s 21(2) of the 1970 Act—and sums paid by an employer by way of contributions to the scheme were allowable as a deductible expense—see s 21(3) of that Act. The relevant provisions were re-enacted as s 592(2) and (4) of the D 1988 Act.

11. The Revenue was required to grant approval if the scheme satisfied the prescribed conditions—that is to say, the conditions set out in s 19(2) of the 1970 Act and Part I of Sch 5 to that Act. The prescribed conditions included, at para (a) of s 19(2), a condition that the scheme was *bona fide* established for the sole E purpose of providing "relevant benefits in respect of service as an employee" and, at para 1 of Sch 5, a condition that the benefits payable to the employee must consist only of benefits payable on or after a specified age not earlier than 60 or later than 70, or on earlier retirement through incapacity. In that context:

> "'relevant benefits' means any pension, lump sum, gratuity or other like benefit given or to be given on retirement or on death, or in anticipation of F retirement, or, in connection with past service, after retirement or death, or to be given on or in anticipation of or in connection with any change in the nature of the service of the employee in question . . ."

and

> "'service' means service as an employee of the employer in question and G other expressions, including 'retirement', shall be construed accordingly;"

Those definitions were found in s 26(1) of the 1970 Act. They have been re-enacted in s 612(1) of the 1988 Act.

12. Approval was mandatory if the scheme satisfied the prescribed H conditions. But discretionary approval could be granted notwithstanding one or more of the prescribed conditions were not satisfied—see s 20(1) of the 1970 Act. The scheme established under the 1980 trust deed did not satisfy the prescribed conditions—if only because the power to pay benefits on early retirement in normal health, conferred by para 2 of sch F to the deed, did not meet the condition in para 1 of Sch 5 of the 1970 Act. Nevertheless, discretionary approval I was given, under s 20(1) of the 1970 Act, with effect from 25 September 1980—see para 2 of the statement of agreed facts. Approval was withdrawn, with effect

from 5 August 1994, under s 591B(1) of the 1988 Act. That followed a decision not to amend the rules of the scheme so as to meet the requirements introduced by the Retirement Benefits Schemes (Restrictions on Discretion to Approve) (Small Self-administered Schemes) Regulations 1991 (SI 1991/1614). But nothing turns on that: the third of the three payments had been made on the previous day, 4 August 1994.

13. Chapter II of Part II of the 1970 Act was repealed by the 1988 Act—see s 844(4) of, and Sch 31 to, that Act. The provisions formerly contained in the 1970 Act were re-enacted as provisions in Chapter I of Part XIV of the 1988 Act. Section 600 of the 1988 Act (which had been introduced by s 21 of, and para 9 of Sch 3 to, the Finance Act 1971) is amongst those provisions. It is relevant to have in mind that other provisions in the 1988 Act have the effect that a lump sum paid to a person on retirement is not chargeable to income tax under Sch E if paid pursuant to an approved scheme, unless it is a payment by way of compensation for loss of office—see ss 148(1), 188(1)(d) and 188(2), 189(a) and 596(1) of the 1988 Act (prior to the Finance Act 1998 amendments). The purpose of s 600(2) of the Act is to bring into the charge to tax under Sch E lump sum payments, not expressly authorised by the rules of an approved scheme, which might otherwise have been thought not to be taxable as emoluments because received after the office or employment had determined.

The scheme

14. Clause 3 of the 1980 trust deed is in these terms, so far as material:

> "The Fund shall be held by the Trustees upon IRREVOCABLE TRUST . . . to apply the income and if and so far as necessary the capital of the Fund in or towards providing relevant benefits as defined in Section 26(1) of the Finance Act 1970 for such Employees of the Employers who become eligible to participate in the Scheme in accordance with the Trust Deed and the Rules."

"Employee" is defined in sch A to the trust deed:

> "'Employee' means a person in the service of the Employer and includes a director".

"Rules" takes its meaning from para 2 of sch D to the trust deed—see the definition in sch A. The paragraph is in these terms, so far as material:

> "Upon an Employee being offered membership of the Scheme a letter with an appendix attached setting out the terms conditions contributions to be made by the Employer and the Employee respectively and benefits to be provided will be drawn up in a form acceptable by the Commissioners of Inland Revenue and signed so as to indicate acceptance by the Employee and by an authorised signatory of the Employer. Upon acceptance the said letter with the appendix attached will be the Rules applicable to such Member . . ."

15. Membership was offered to Mr. Venables by a letter dated 25 September 1980. That letter, and the appendix attached to that letter, constituted

A the Rules applicable to him. The following provisions in the appendix are material:

"1. Contributions

The whole cost of the Scheme will be met by the Company. Each year the Company will pay contributions into the Scheme to build up a capital sum in order to provide your retirement and other benefits ('Your Capital Sum'). The amount of each year's contributions will be determined by the Company.

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2. Normal Retirement

You will normally retire from the Company's service on 13 December, 2000, your Normal Retirement Date, when you will be aged 60 years and you will have been a member of the Company for more than 20 years.

C

On your Normal Retirement Date Your Capital Sum will be realised to provide your retirement benefits. Shortly before that date you will be advised of the amount of Your Capital Sum and the pension it will purchase. You may elect to take part of Your Capital Sum in the form of a tax free cash sum of up to a maximum of 150% of your Final Remuneration as defined in the Trust Deed. . . .

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. . .

5. General Conditions

The following paragraphs describe the general conditions relating to the payment of your benefits. However it is the Trust Deed which governs these conditions and it will always take precedence over this Rule.

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(a) Retirement before Normal retirement Date

With the Company's consent you may retire at any time after age 50. At the date of actual retirement, Your Capital Sum in the Scheme would be realised to provide reduced benefits. . . .

(d) Limit on Benefits

F

The Scheme is designed to be approved by the Inland Revenue as an exempt approved scheme under the 1970 Finance Act. One of the conditions of approval is that your total benefits from this or any other pension arrangement must not exceed the maximum benefits specified by the Inland Revenue. Those maximum benefits are defined in the Trust Deed".

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16. As I have said, the benefits payable under the scheme are set out in sch F to the trust deed. Paragraph 1 of sch F provides that, subject to paras 4 and 5, the benefits which a member shall be entitled to receive on retirement at Normal Retirement Date are "such benefits as are stated in the Member's Rules". In the case of Mr. Venables, that means whatever benefits can be provided out of the capital sum built up by such contributions as the company might, from year to year, decide to make; but subject to the restriction that the total benefits from the scheme and any other pension arrangements must not exceed the maximum benefits specified by the Inland Revenue. Paragraph 2 of sch F gives the power to pay an immediate pension to a member who retires in normal health at or after age 50 which I have already set out. The paragraph continues:

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"The amount of pension will be calculated as for deferred pensions (see Clause 4 of Schedule G) and will then be reduced by such a proportion as

the Actuary determines having regard to the Member's age at actual retirement but in no case greater than the amount which would prejudice the Scheme as an exempt approved scheme under Chapter II of Part II of the Finance Act 1970 . . ." A

17. Schedule G to the Trust Deed sets out the entitlement of a member to "Short Service Benefits". Short Service Benefits are payable, at Normal Retirement Date, in respect of a member "who leaves Service before his Normal Retirement Date"; and they take the form of a deferred pension or a transfer into another scheme—see paras 3 and 9 of sch G and (as to transfers) sch I. The benefits paid to Mr. Venables in the present case were not Short Service Benefits under sch G. But, under the provisions in para 2 of sch F which I have set out, para 4 of sch G was of relevance to the calculation of his retirement benefits on early retirement. Paragraph 4 of sch G provides, so far as material, that where the benefits at Normal Retirement Date prescribed in the Rules applicable to the member are expressed in the form of a capital sum (as they were in the Rules applicable to Mr. Venables) the deferred pension payable under the scheme is to be equal to the member's interest in the Fund. The effect was that (as Rule 5(a) of the Rules applicable to him had indicated) the benefits payable to him under para 2 of sch F on early retirement were the benefits that could be provided under the capital sum which had built up out of the company's contributions. But, again, that was subject to the maximum benefits restriction. B C D

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18. Paragraph 4 of sch F defines the maximum benefits. The basic rule is that the pension of a member at Normal Retirement Date shall not exceed two-thirds of his Final Remuneration. Part of that pension may be taken as a commuted lump sum—see para 5 of sch F—but subject to a maximum (after 20 years service) of 120/80ths of Final Remuneration. Final Remuneration, therefore, is an important concept. It controls both the amount of the pension that can be provided and the amount that can be commuted and taken as a tax free lump sum. It is defined in s 612(1) of the 1988 Act to mean the average annual remuneration of the last three years' service. But, in the context of the scheme, it has a different and more extensive meaning—see the definition in sch A to the trust deed: F

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"'Final Remuneration' means the greater of (i) . . . or (ii) the average of Increased Total Emoluments for any three or more consecutive years ending not earlier than ten years before the date of retirement leaving Service or death . . ."

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In the case of a member who is a director of the employer company and who, in conjunction with any settlement to which he has transferred shares, can exercise more than 20 per cent. of the votes exercisable by shareholders in that company (which Mr. Venables was in June 1994) Final Remuneration is to be measured by sub-para (ii) of the definition which I have just set out—see para 4B in sch F to the trust deed. Increased Total Emoluments in respect of any year means the total emoluments received in that year increased by indexation. I

A **The approach to construction**

19. I have set out the provisions of the scheme in some detail because they demonstrate—as clearly as may be—the need to read the scheme in conjunction with the provisions in Chapter II of Part II of the 1970 Act. The object of the scheme is to provide "relevant benefits" within the meaning of those provisions;
B that is to say, benefits given or to be given "on retirement . . . or in anticipation of retirement . . . or . . . in connection with any change in the nature of the service of the employee in question"—see s 26(1) of the 1970 Act (now s 612(1) of the 1988 Act). The amount of the benefits is capped by para 4 of sch F of the trust deed so as not to prejudice "the approval of the scheme as an exempt approved scheme under Chapter II Part II of [the 1970 Act]". The Rules applicable to Mr.
C Venables, at Rule 5(d), refer to the restriction on benefits as "one of the conditions of approval" as an exempt approved scheme. With those provisions in mind, it seems to me that—in the absence of some strong contra-indication— the parties to the trust deed must be taken to have intended that words and expressions in the trust deed should be construed in the same sense as that in which the same words and expressions would be understood in the context of the
D legislative provisions under which approval of the scheme established by the trust deed was to be sought. It must be kept in mind that the trust deed was executed with the intention that the scheme which it established would be put before the Inland Revenue for approval under s 20(1) of the 1970 Act. As Warner J. observed, in *Mettoy Pension Trustees Ltd.* v. *Evans and others* [1990] 1 WLR 1587, at p 1610H:

E "... as was common ground, pension scheme documents have to be construed in the light of the requirements of the Inland Revenue Commissioners from time to time for their approval of a scheme . . ."

The Revenue, at least, could be expected to decide whether or not to approve the scheme on the basis that words and expressions in the trust deed
F were intended to be construed in the context of the legislative provisions unless it was made clear that that was not the parties' intention. If the parties intended otherwise, it was for them to say so.

20. It is relevant, therefore, to ask what meaning should be given to the word "retire" in the context of the legislative provisions contained in Chapter II of Part
G II of the 1970 Act. The meaning to be given to the word in the context of the legislative provisions is relevant, although not necessarily determinative, because (as I have said) in the absence of some strong indication to the contrary, the parties must be taken to have intended a word which describes a concept of such obvious importance in relation to the payment of benefits under approved schemes to bear the same meaning in the context of the scheme.

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The meaning of "retire" in the legislation and the scheme

21. The starting point, as it seems to me, is the direction, in the definition of "service" in s 26(1) of the 1970 Act, that "other expressions, including 'retirement', shall be construed accordingly". "Service" means service as an
I employee of the employer in question. It must follow that "retirement" means "retirement from service as an employee of the employer in question". It does not

mean or include "change in the nature of service as an employee of the employer in question". That is confirmed by the distinction, in the definition of "relevant benefits", between benefits "given on retirement" or "in anticipation of retirement" and benefits given "on or in anticipation of or in connection with any change in the nature of service". The definition of "relevant benefits" in s 26(1) of the 1970 Act makes it clear that, although "benefits given on retirement" and "benefits given on any change in the nature of service" are both within it, the two concepts are not the same. If "retirement from service" does not mean or include "change in the nature of service" then—as it seems to me—the only meaning which can be given to that expression is "cessation of service". I would hold that, in the context of the legislative provisions, "retirement" means cessation of service as an employee of the employer in question; and "retire" must be construed accordingly.

22. The next step is to ask what is meant by "service as an employee of the employer in question". Again, the answer is provided by s 26(1) of the 1970 Act. "Employee", in relation to a company, includes any director of the company. So service as an employee of the company in question must include the holding of the office of director of that company. And it must follow that there is no cessation of service as an employee of the company in question for so long as the director continues to hold that office. That does not lead to the conclusion that relevant benefits under an approved scheme cannot be provided to a managing director or chief executive who, on ceasing to have an executive role, continues as a non-executive director. But it does lead to the conclusion that, if a managing director or chief executive is to be awarded a pension or lump sum in those circumstances, that is a benefit given in connection with a change in the nature of his service, not on his retirement from his service with the employer in question.

23. The third step is to ask whether the concept of "retirement" under the scheme is be understood in a different sense from "cessation of service": in particular, whether, in the context of the scheme, that concept was intended to include a change in the nature of the employee's service. The definitions in sch A to the trust deed do not suggest an affirmative answer. "Service", in the context of the scheme, means "service with an employer for the purposes of the Trust Deed and the Rules". "Employee" means "a person in the service of the Employer and includes a director". "Relevant Employment" means "the employment in respect of which an individual is a Member of this Scheme". The important concept of "Final Remuneration" is defined in terms which recognise a distinction between "retirement" and "leaving Service"; but that is explained by the distinction between benefits payable on retirement under sch F and Short Service Benefits payable under sch G. "Leaving Service" is, plainly, synonymous with "cessation of service"; but that does not lead to the conclusion that "retirement" is not also to be understood in that sense. An employee whose service ceases before Normal Retirement Date will, in the ordinary case, be treated as "leaving Service" for the purposes of an entitlement to "Short Service Benefits" under sch G; but he may, exceptionally (as in the case of Mr. Venables), be treated as having "retired" for the purposes of an entitlement to an immediate pension on early retirement under sch F. The apparent distinction between "retirement" and "leaving Service"—recognised in the definition of "Final Remuneration" and incorporated in the respective provisions of schs F and G—provides no support for a conclusion that "retirement" is to be understood, in the context of the scheme, in any sense other than "cessation of service".

A 24. For my part, I would not exclude the possibility that the Rules applicable to a particular employee might define his "Relevant Employment"—that is to say, the employment in respect of which that employee is admitted to membership of the scheme—in such a way as to confine his service with the employer in question to service in a particular role. So, for example, the Rules applicable to him might have the effect that his service, for the purposes of the B scheme, was service as an executive under a contract of service. In such a case, service would cease on termination of his contract of service; notwithstanding that he continued as a non-executive director. But that is not this case. There is nothing in the letter of 25 September 1980, or its attachment, which has the effect of confining Mr. Venables' service with the company to service in a particular role. Indeed, there is nothing in the Commissioner's findings to suggest that Mr. C Venables ever had a contract of service under which he was employed in an executive role.

25. It follows that I would decide the principal issue against the taxpayers. In my view the payments were not authorised by the Rules because they were not made to a member who retired within the meaning of para 2 of sch F to the trust D deed or para 5(a) of the attachment to the letter of 25 September 1980.

The secondary issue: were the payments made at all?

26. This issue, as the Judge recognised, did not arise on the appeals before him in the circumstances that he had held that the payments were authorised by E the rules of the scheme. Nevertheless the issue had been argued before him and he addressed it in his judgment. He summarised the argument advanced on behalf of the taxpayers in four propositions: (a) if the payment to Mr. Venables was not authorised by the trust deed or the rules, then he was not beneficially entitled to it; (b) Mr. Venables was a trustee of the scheme, and if he was not entitled to the payment, he could not have taken it free from the trusts of the F scheme; (c) consequently, the money remained subject to the trusts of the scheme, and nothing accrued to Mr. Venables; (d) accordingly he received nothing and there was therefore no payment to him.

27. In my view, that argument was plainly untenable. Section 600 of the 1988 Act imposes a charge to tax in circumstances where (i) a payment to or for G the benefit of an employee (otherwise than in course of payment of a pension) is made out of funds which are held for the purposes of an approved scheme and (ii) the payment is not expressly authorised by the rules of the scheme. In those circumstances the employee is chargeable to tax on the amount of the payment (whether or not he was the recipient of the payment). It is axiomatic that monies or property transferred in breach of trust out of funds subject to a trust will, for H so long as they are identifiable, continue to be subject to that trust until they come into the hands of a *bona fide* purchaser for value without notice of the equity to trace—see *Snell's Equity* (30th edition, 2000) at paras 13–41, pp 340–1. To hold that there had been no payment because the monies paid remained subject to the trusts of the scheme would be to defeat the obvious purpose of the taxing provision. It could not have been the intention of the legislature that the question I whether or not a charge to tax arose under s 600(2) of the 1988 Act would turn upon an investigation whether or not there remained out of the monies or

property transferred some monies or property which (into whoever's hands they might have come) were still subject to the trusts of the scheme. A

28. The Judge did not, I think, accept the argument in the stark terms in which it was advanced. But he would have been prepared to hold (had the point arisen) that there was no payment for the purposes of s 600 of the 1988 Act if three conditions were fulfilled: (i) that the payment was in breach of trust, (ii) that the recipient is accountable to the trustees as an actual or constructive trustee, and (iii) that the recipient is able and prepared to account to the trustees—see para 37 of the judgment which he handed down on 14 June 2001. He found support for that formulation in the decision of Arden J. in *Hillsdown Holdings plc* v. *Inland Revenue Commissioners* (1999) 71 TC 356; [1999] STC 561. B C

29. In the *Hillsdown Holdings* case, the company and the trustees of its pension scheme sought repayment of tax charged and paid under s 601 of the 1988 Act. The section is in these terms, so far as material:

> "(1) Subsection (2) below applies where a payment is made to an employer out of funds which are or have been held for the purposes of a scheme which is or has at any time been an exempt approved scheme and whether or not the payment is made in pursuance of Schedule 22 [reduction of pension fund surpluses]. D
>
> (2) An amount equal to 40 per cent. of the payment shall be recoverable by the Board from the employer." E

30. The relevant facts may be stated shortly. Following the acquisition by Hillsdown of the FMC group of companies, surplus assets in the FMC pensions scheme were transferred to the HF pensions scheme in respect of which Hillsdown was the employer. As a result of that transfer the HF scheme was found to be in surplus. The Revenue approved a reduction of that surplus, under sch 22 to the 1988 Act, and a payment was made to Hillsdown. Tax was charged and paid under s 601 of the Act. There was no power, under the FMC scheme, to transfer surplus assets to an employer on winding up and no power to introduce such a power by amendment; but a power to that effect had been introduced into the HF scheme. It was subsequently held, on a complaint by a member of the FMC scheme, that the FMC trustees had been in breach of trust in transferring surplus assets to the HF trustees in the knowledge that those assets would, indirectly, be returned to the employer. Hillsdown was ordered to repay to the HF trustees the monies which it had received. It did so, after deduction of the tax already paid under s 601 of the Act. The issue before Arden J. was whether the Revenue were liable to repay the tax. That turned on whether the payment which had been (but which ought not to have been) made by the HF trustees to Hillsdown was a payment for the purposes of s 601 of the Act. She held that it was not. F G H

31. The kernel of Arden J.'s reasoning in the *Hillsdown Holdings* case (1999) 71 TC 356; [1999] STC 561—at least for present purposes—is to be found, I think, in a passage at [1999] STC 561 at p 571 h-j. After expressing the view (*ibid*, at a-b) that "there is no reason in the present case why Parliament should seek in s 601 to tax a payment which was not effectively made" and that the policy of the sections would suggest otherwise, she said this: I

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> "Further support . . . is to be found in s 601(1) itself: the payment must be 'out of' the fund. In my judgment, these words indicate that the payment must result in funds effectively leaving the fund as intended by the transaction (whether absolutely or for a period, as in the case of a loan). The words 'out of' are not apt to describe a payment which, contrary to the stated effect of the transaction, does not have the effect of changing the ownership of the monies paid and is in fact reversed. Likewise, under s 601, the payment must be made 'to an employer' and this must mean in the employer's capacity as such and exclude the case where the employer merely receives the moneys as a trustee under a trust arising under operation of law for the fund."

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32. If it were necessary to do so, the Revenue would contend that the *Hillsdown Holdings* case was wrongly decided and invite this Court to overrule that decision. But their primary submission is that that is not necessary; the present case can be distinguished. In my view they are correct in that submission. The charge to tax under s 601 of the 1988 Act arises whenever a payment is made to an employer out of funds which are or have been held for the purposes of an exempt approved scheme. The object of that taxing provision—as counsel for Hillsdown had submitted and Arden J., I think, accepted—was "in a rough-and-ready way" to reverse the tax advantage which an employer would otherwise obtain if there were repaid to it, free of tax, monies derived from contributions which it had made into an exempt approved scheme—see [1999] STC 561 at p 567 a-b. It must be kept in mind that the employer will have obtained tax relief in respect of its contributions; and that (as the law then stood) the investment income generated in the pension fund would be exempt from tax. So, if surplus assets are repaid to the employer, there must be a tax charge. It is also necessary to keep in mind that an employer's scheme may be expected to contain provision for the return of surplus assets (after actuarial certification) and that s 603 of the 1988 Act, and sch 22, provide for the making of regulations in relation to the reduction or repayment of surpluses. It is to be expected that payments which attract tax under s 601 of the Act will be payments which are authorised by the scheme rules and comply with sch 22 and the regulations. The unauthorised payment is likely to be the exception. Effect can be given to s 601 of the 1988 Act on the basis that unauthorised payments are not to be treated as payments at all—as Arden J. decided.

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33. By contrast, the charge to tax under s 600 of the 1988 Act arises only where the payment is unauthorised and in breach of trust. If an unauthorised payment is to be treated as no payment at all, the section is self-defeating. That cannot have been Parliament's intention. The Judge in the present case sought to avoid that difficulty by identifying the three conditions which I have set out. But, to my mind, those conditions do not meet the difficulty. The first of those conditions—(i) that the payment was in breach of trust—is a restatement of the premise upon which a charge to tax under s 600 arises. The second condition—(ii) that the recipient is accountable to the trustees as an actual or constructive trustee—is likely to be satisfied in any case in which the recipient has not disposed of all the monies paid to him before the breach of trust is brought to his

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knowledge; and it leads to the conclusion that he is not taxable in respect of the monies of which he had disposed, but (potentially) is taxable in respect of those which he had retained. The third condition—(iii) that the recipient is able and prepared to account to the trustees—leads to the conclusion that the question whether or not a payment has been made depends on the state of mind (and the financial position) of the recipient after the event.

34. The point can be illustrated by an example. Suppose A receives a lump sum out of the scheme funds on 1 January. On 1 July it is discovered that that sum was paid in breach of the rules. A is not willing to accept there has been a breach of the rules, and wishes to take legal advice. At that stage, applying the Judge's third condition, the payment is treated as a payment for the purposes of s 600 of the Act. On 1 October, after taking advice, A accepts that he should repay the monies; but is not then in a position to do so. Again, applying the Judge's third condition, the payment made on 1 January is still treated as a payment for the purposes of s 600 of the Act. On 1 December the Revenue make an assessment on A in respect of the monies received in the previous year of assessment. Applying the Judge's third condition, that assessment is properly made at the time. Six months later, on 1 June in the following calendar year, A receives a windfall and is then in a position to make repayment. He remains willing to do so. The effect of the Judge's third condition is that what has been, for the previous eighteen months, properly treated as a payment for the purposes of s 600 of the 1988 Act (and has given rise to a valid assessment to tax under that section) has ceased to be a payment for those purposes. And the position is the more bizarre if it is supposed that, on 1 September in the second year, before A has actually made any repayment, he falls on hard times (or finds some other pressing need for the money) and is no longer in a position to do so. Is the payment of 1 January once again to be treated as a payment for the purposes of s 600 of the Act? The Judge's third condition requires an affirmative answer. I cannot believe that Parliament intended that the question whether a charge to tax has arisen should depend on the state of mind and financial position of the taxpayer after the event.

35. Further, there is, of course, the evidential difficulty, in the present case, that the Special Commissioner has made no finding whether Mr. Venables is willing and able to repay to the trustees the monies paid to him in 1994. In the circumstances that the scheme has ceased to be an exempt approved scheme, it cannot be assumed that he would be. What the position would have been if Mr. Venables had repaid to the trustees the monies paid to him before any assessment had been made does not arise for decision in the present case.

36. I would decide the secondary issue against the taxpayers. In my view the payments made to Mr. Venables in July and August 1994 were payments "made out of funds held for the purposes of [the scheme]" to which s 600 of the 1988 Act applied.

A **Conclusion**

37. I would allow this appeal.

Potter L.J.:—

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38. I agree.

Peter Gibson L.J.:—

39. Although we are differing from the conclusions of the Judge and from C the reasoning of the Special Commissioner, there is nothing which I would wish to add to Chadwick L.J.'s comprehensive judgment with which I am in entire agreement.

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The taxpayers' appeal was heard in the House of Lords before Lord Nicholls of Birkenhead, Lord Slynn of Hadley, Lord Millett, Lord Scott of Foscote and Lord Walker of Gestingthorpe on 2 October 2003 when judgment was reserved. On 4 December 2003, judgment was given against the Crown, Lord Walker of Gestingthorpe dissenting, with costs.

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Conrad McDonnell for the taxpayers.

Timothy Brennan Q.C. and *Ingrid Simler* for the Crown.

The cases referred to in the speeches are as follows; *Brock* v. *Bradley* (1864) F 33B 670; *Harris* v. *Lord Shuttleworth* [1994] ICR 991; *Hillsdown Holdings plc & another* v. *Commissioners of Inland Revenue* (1999) 71 TC 356; [1999] STC 561; *Jones* v. *Westcomb* (1711) Prec. Ch. 316; *Mettoy Pension Trustees Ltd.* v. *Evans & others* [1990] 1 WLR 1587; [1991] 2 All ER 513; *Re Courage Group's Pension Schemes, Ryan & others* v. *Imperial Brewing & Leisure Ltd.* [1987] 1 All ER 528; *Secretary of State for Trade & Industry* v. *Bottrill* [2000] 1 All ER 915.

G The cases cited in argument, in addition to those referred to in the speeches, are as follows; *Air Jamaica Ltd. & others* v. *Charlton & others* [1999] 1 WLR 1399; *Bartlett & others* v. *Barclays Bank Trust Co. Ltd.* [1980] Ch 515; [1980] 2 WLR 430; [1980] 1 All ER 139; *Carmichael & another* v. *National Power plc* [1999] 1 WLR 2042; [1999] 4 All ER 897; *Clark* v. *Oxfordshire Health Authority* [1998] IRLR 125; *Cooke (HMIT)* v. *Blacklaws* (1984) 58 TC 255; [1985] STC 1; *Cowan* H *& others* v. *Scargill & others* [1985] Ch 270; [1984] 3 WLR 501; [1984] 3 All ER 750; *DTE Financial Services Ltd.* v. *Wilson (HMIT)* (2001) 74 TC 14; [2001] STC 777; *Eaton* v. *Robert Eaton Ltd.* [1988] ICR 302; *Edwards (HMIT)* v. *Bairstow & another* [1956] AC 14; (1955) 36 TC 207; [1955] 3 WLR 410; [1955] 3 All ER 48; *Folami* v. *Nigerline (UK) Ltd.* [1978] ICR 277; *Foskett* v. *McKeown & others* [2001] 1 AC 102; (2001) 73 TC 1; [2001] 2 WLR 377; [2000] 3 All ER 97; *Henry* I *(HMIT)* v. *Galloway* (1933) 17 TC 470; *Hoover Ltd.* v. *Hetherington* [2002] EWHC 1052 (Ch); *Imperial Group Pension Trust Ltd. & others* v. *Imperial*

Tobacco Ltd. & others [1991] ICR 524; [1991] 1 WLR 589; [1991] 2 All ER 597; *In re Barings plc & others* (No. 3) [2000] 1 WLR 634; [1999] 1 All ER 1017; *In re Lucking's Will Trusts* [1968] 1 WLR 866; *MacNiven (HMIT)* v. *Westmoreland Investments Ltd.* [2003] 1 AC 311; (2001) 73 TC 1; [2001] 2 WLR 377; [2001] 1 All ER 865; [2001] STC 237; *Market Investigations Ltd.* v. *Minister of Social Security* [1969] 2 QB 173; [1969] 2 WLR 1; *National Grid plc* v. *Mayes & others* [2001] 1 WLR 864; [2001] 2 All ER 417; *O'Kelly & others* v. *Trusthouse Forte plc* [1984] QB 90; [1983] 3 WLR 605; [1983] 3 All ER 456; *Oliver* v. *Chuter (HMIT)* (1934) 18 TC 570; *Parry* v. *Cleaver* [1970] AC 1; [1969] 2 WLR 821; [1969] 1 All ER 555; *Parsons* v. *Albert J Parsons & Sons Ltd.* [1979] ICR 271; *Perrot* v. *Supplementary Benefits Commission* [1980] 1 WLR 1153; [1980] 3 All ER 110; *R* v. *Inland Revenue Commissioners* ex parte *Roux Waterside Inn Ltd.* (1997) 70 TC 545; [1997] STC 781; *Rose* v. *Humbles (HMIT)* (1971) 48 TC 103; [1972] 1 WLR 33; [1972] 1 All ER 314; *Sidey* v. *Phillips (HMIT)* (1986) 59 TC 458; [1987] STC 87; *Taupo Totara Timber Co. Ltd.* v. *Rowe* [1978] AC 537; [1977] 3 WLR 466; [1977] 3 All ER 123; *Vandyk* v. *Minister of Pensions and National Insurance* [1955] 1 QB 29; [1954] 3 WLR 342; [1954] 2 All ER 723.

Lord Nicholls of Birkenhead

My Lords,

1. I have had the advantage of reading in draft the speech of my noble and learned friend Lord Millett. For the reasons he gives, with which I agree, I would allow this appeal.

Lord Slynn of Hadley

My Lords,

2. I have had the advantage of reading in draft the opinion of my noble and learned friend Lord Millett. I agree that the appeal should be allowed for the reasons he gives.

Lord Millett

My Lords,

3. In March 1997 the Appellant taxpayer was assessed to income tax in respect of three payments totalling £580,591 made to him in July and August 1994 from the funds of his pension scheme. The assessment was made under s 600(2) of the Income and Corporation Taxes Act 1988 as amended by the Finance Act 1989. Section 600 provides:

> "(1) This section applies to any payment to or for the benefit of an employee, otherwise than in course of payment of a pension, being a payment made out of funds which are held for the purposes of a scheme

A which is approved for the purposes of . . . (b) Chapter II of Part II of the Finance Act 1970. . . .

(2) If the payment is not expressly authorised by the rules of the scheme . . . the employee . . . shall be chargeable to tax on the amount of the payment under Schedule E for the year of assessment in which the payment is made."

B 4. It is common ground that the payments were made from funds which were held for the purposes of an approved pension scheme. The Revenue claim that the payments were not "expressly authorised by the rules of the scheme" because, at the time they were made, the taxpayer remained a director of one of the participating employers in the scheme and so (it is said) had not "retired" within the meaning of the rules. It is not disputed that when the payments were C made the taxpayer was still a non-executive director of a participating employer. The principal issue in this appeal is whether it follows that the taxpayer had not "retired" within the meaning of the rules of the scheme so that the payments were unauthorised (for nothing seems to turn, at least in this case, on the word "expressly").

D 5. A secondary issue is whether, if the payments were unauthorised, they should be treated for tax purposes as if they had not been made. The taxpayer contends that if the payments were not authorised then, as one of the trustees of the scheme, he received and held them throughout as a constructive trustee on the trusts of the scheme. It is common ground that if the payments were not authorised then, unless they can be treated as not having been made (or at least not made "out of" the funds of the scheme), the assessment was properly made.

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The proceedings

6. The taxpayer's appeal against the assessment was dismissed by the single Special Commissioner on the ground that, although the taxpayer had "retired", he had not retired "in normal health" as required by the rules of the scheme. On F the taxpayer's appeal and the Revenue's cross-appeal the Judge (Lawrence Collins J.) [2002] ICR 81 upheld the Commissioner's finding that the taxpayer had retired but reversed his finding that he was not then in normal health and discharged the assessment. On appeal to the Court of Appeal the Revenue did not challenge the Judge's conclusion that he had been in normal health at the relevant time but continued to maintain that the taxpayer had not retired. The G Court of Appeal [2003] ICR 186 allowed the Revenue's appeal and held that at the time the payments were made the taxpayer had not retired because he continued in office as a non-executive director. It also held that although the payments, being unauthorised, were made in breach of trust, they were not to be treated as if they had not been made.

H **The facts**

7. The Fussell Pension Scheme ("the scheme") was established by a Trust Deed ("the trust deed") dated 25 September 1980 as an occupational pensions scheme for the benefit of directors and employees of Fussell Estates Ltd. and other participating employers. The scheme was approved by the Commissioners

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of Inland Revenue with effect from the same date. At all material times it was an exempt approved scheme. On 26 May 1989 the terms of the trust deed were amended so that thereafter Ven Holdings Ltd. ("the company") was treated as the founder of the scheme in place of Fussell Estates Ltd. With effect from that date the participating employers under the scheme were the company and Fussell Estates Ltd. The taxpayer and a trust corporation were the trustees of the scheme. At all material times the taxpayer held approximately 20 per cent. of the shares in the company and the remaining 80 per cent. of the shares were held by a family discretionary trust of which the taxpayer was the settlor and one of the trustees.

8. The company, which had a number of subsidiaries, was engaged in the construction industry. The taxpayer, who was a carpenter by trade, was aged 53 in June 1994. In the early days he had worked on building sites, though he had not done so for many years. He had worked for the company for upwards of 30 years, and had for some time been an executive director and chairman of the company, in which capacity he worked about 30 hours a week and was paid some £25,000 per annum.

9. In March 1993 the group's managing director retired and the taxpayer's workload increased so that he worked nearly 50 hours a week. He became responsible for the day to day running of the group and, although never formally appointed as such, he undertook the functions previously performed by the group's managing director. The Commissioner described him as having "stepped into the gap" left by the retirement of the former managing director without any formality.

10. On 23 June 1994 a board meeting of the company took place at which it was resolved that the taxpayer:

> "will be retiring as an executive director on 30 June 1994 to pursue other interests but will continue as an unpaid non-executive director."

In a letter of the same date the taxpayer notified the other trustee of the scheme that he would be retiring from employment with the group from 30 June 1994 and that he wanted to take most of his lump sum pension entitlement from the scheme in the form of property.

11. The Commissioner found that after 30 June 1994 the taxpayer was an unpaid non-executive director of the company and ceased to be an employee, not having even an oral contract. He now spent a large part of his time in the USA, buying a house in Florida in May 1996, though he returned to the United Kingdom from time to time. He was still a major shareholder and the remaining shares were held by a family trust which he had established. He naturally maintained an interest in the company's affairs and continued to give advice—usually by telephone—to those now running the company, but he received no remuneration for doing so. He no longer visited building sites or normally attended the office. He was for the most part physically absent being, as the Commissioner put it, "not an hour's drive from the business, but on the other side of the Atlantic."

A 12. The Commissioner found that the taxpayer, who suffered from a heart condition, (i) was not in normal health on 30 June 1994 (as I have explained, this finding was reversed on appeal); (ii) did not retire from the office of managing director, because he had never been appointed to it; but (iii) did retire from employment with the company and from normal service on its behalf. When discussing the relevant statutory provisions the Commissioner later recorded B that it was "common ground" that the taxpayer was a director both before and after 30 June 1994 and an employee before that date. This was not entirely correct. In the absence of any written contract of employment the Revenue has not accepted that he was ever an employee of the company.

The Fussell Pension Scheme

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13. The scheme was a contributory final salary pension scheme of a familiar kind. The trust deed recited that it had been decided to establish a scheme for providing "relevant benefits as defined in section 26(1) of the Finance Act 1970" for eligible "directors and employees" of participating companies.

D 14. Consistently with the recitals clause 3 of the trust deed provided that the funds of the scheme were to be held on trust for the provision of "relevant benefits as defined in section 26(1) of the Finance Act 1970" for eligible "employees"; and "employee" was defined as meaning: "a person in the service of [the company] and includes a director".

E 15. "Normal retirement date" was defined as the date stated in the rules applicable to the particular member. In the taxpayer's case this was stated to be 13 December 2000, when he would be aged 60 and would have been a member of the company for 20 years. On retirement at normal retirement date a member became entitled to a pension in accordance with the rules applicable to him. In the taxpayer's case he was entitled to elect to take part of his benefit in the form of a tax-free capital sum not exceeding 150 per cent. of his final remuneration.

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16. Clause 2 of sch F to the trust deed made provision for early retirement. This gave the trustees a discretion exercisable with the consent of the company:

> "to award an immediate pension to a member who retires in normal health at or after age 50."

G The rules applicable to the taxpayer provided that with the company's consent he might retire with reduced benefits at any time after age 50. It was, however, expressly stated that the trust deed governed the matter and that it would always take precedence over the rules.

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The statutory provisions

17. It will be recalled that under the terms of the trust deed the fund was to be held in trust for the provision of retirement benefits as defined by s 26(1) of the Finance Act 1970 for the benefit of employees (which term included directors). So far as material s 26(1) of the 1970 Act defines "relevant benefits" as meaning:

> "any pension, lump sum, gratuity or other like benefit given or to be given on retirement or on death, or in anticipation of retirement, or, in connection with past service, after retirement or death, or to be given on or in anticipation of or in connection with any change in the nature of the service of the employee in question . . ."

The section also defines "employee" in relation to a company for the purpose of the relevant part of the 1970 Act as including:

> "any officer of the company, any director of the company and any other person taking part in the management or the affairs of the company".

Was the taxpayer entitled to retirement benefits on early retirement in ill health?

18. This is no longer a live issue because the Judge reversed the Commissioner's finding that, at the date of his retirement, the taxpayer was not in normal health. It would be remarkable if on its true construction the trust deed provided for a pension to be paid on early retirement to a member who was in normal health but not to a member who was in ill health. The trust deed continues in operation and will apply to members who take early retirement in future, so that the construction which the courts have placed upon it will affect others besides the taxpayer. In these circumstances I think that I should briefly explain why I consider that the trust deed does not have this effect.

19. The Commissioner reasoned as follows:

(i) the rules make provision for discretionary benefits to be payable to a member on retirement at or after the age of 50 without any reference to the state of his health;

(ii) where there is a conflict between the trust deed and the rules the trust deed prevails;

(iii) the trust deed permits payment of benefits on early retirement only if two conditions are satisfied: (a) the member must have retired and (b) he must have done so in normal health;

(iv) early retirement on grounds of ill health is therefore a *casus omissus.*

20. Thus the Commissioner treated the words "in normal health" as a qualifying condition which must be satisfied before a member can become eligible for benefit on early retirement. It is most unlikely that it was not intended to cover early retirement in ill health, since this is an a fortiori case; and the Commissioner accordingly took it to be an inadvertent *casus omissus.* A more plausible construction of the words "in normal health", however, is to treat them, not as words of limitation, but as words of exposition. Read in this way they refer

A to a member "who retires (even in normal health) at or after the age of 50." Such a construction has the advantage, not only of producing what must have been the intended result, but also of eliminating any conflict between the rules and the trust deed. It would, moreover, accord with the principle (once known as "the rule in *Jones* v. *Westcomb* (1711) Prec. Ch. 316") that a gift on a contingency which does not occur nevertheless takes effect on the happening of an event B which is a fortiori. Thus a legacy to a single woman if she survives her husband takes effect if she never marries: see *Brock* v. *Bradley* (1864) 33 B 670; and a gift over in the event of a prior legatee having only one child takes effect if the prior legatee has no child: *Murray* v. *Jones* (1813) 3 Ves & B 313. The further contingency arises by necessary implication to give effect to the evident intention of the grantor.

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Was the taxpayer an employee?

21. The taxpayer was certainly an employee within the meaning of both the trust deed and the Finance Act 1970, since they both define the expression as including a director. The Revenue accept that he was a director before 30 June D 1994 and remained a director after that date. But they deny that he was ever an employee.

22. Whether the taxpayer was an employee of the company is a question of fact. The Commissioner found that he was. He found in terms that the taxpayer "did retire from employment with the company" and that after 30 June 1994 he E "was an unpaid non-executive director, and ceased to be an employee". There was abundant evidence to support his conclusion, for the taxpayer had worked for the company for many years and latterly carried out the functions performed by a managing director, and was paid for doing so. Having regard to the nature of the company as a small family company, it is not surprising to find that he never had a written contract. There is no evidence to suggest that he was paid director's fees; and the fact that he ceased to be paid anything when he became F a non-executive director is strong evidence that he had been paid for the work he did as an employee and not for the responsibilities he undertook as a director. Given the hours he worked before June 1994 and the extent of his duties as a director of a small family company, it is far-fetched to attribute his remuneration to his office rather than his employment.

G 23. It should be borne in mind that the absence of a written contract and the character of the company as a small family company, while not irrelevant, are far from conclusive on the question. There is no rule of law which precludes even a sole or controlling shareholder from being an employee of a company, and the taxpayer was neither. While the degree of control is always significant and might on occasion be decisive, it is only one of the relevant factors to be taken H into account in considering whether there is a genuine contract of employment. The fact that the person claiming to be an employee is the controlling shareholder and ultimately has the power to prevent his own dismissal does not prevent the existence of a genuine contract of employment: see *Secretary of State for Trade and Industry* v. *Bottrill* [2000] 1 All ER 915 CA.

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Did the taxpayer "retire"? A

24. The Court of Appeal accepted the Revenue's argument that the taxpayer did not "retire" within the meaning of the 1970 Act. On a careful analysis of the provisions of the 1970 Act, it reasoned that "retirement" means "retirement from service as an employee" and did not extend to a change in the nature of the service as an employee. It then asked what is meant by "service as an employee" and answered it by reference to the provisions of s 26(1) of the 1970 Act, which defines "employee" in relation to a company as including any director of the company. Accordingly, it reasoned, service as an employee of the company must include service as a director of the company, and it followed that there is no retirement from service as an employee for so long as the person in question continues to hold office as a director. B C

25. Strictly speaking the question turns on the meaning of the word "retire" in the trust deed and not in the Finance Act 1970, but there is no material difference between them for present purposes and nothing turns on this. Both contain the critical definition of "employee", which lies at the heart of the Revenue's case and the reasoning of the Court of Appeal. D

26. I would for my part accept the reasoning of the Court of Appeal with the exception of the last step. In my opinion it does not follow from the fact that the word "employee" is defined to include a director that an employee who is also a director must retire from both his employment and his office as director before he can be said to "retire" within the meaning of the trust deed. E

27. A definition clause is principally a drafting device employed to avoid unnecessary repetition and applies only for the purpose of construing the document or part of the document in which it is contained. Unfortunately the use of a definition as shorthand in this way sometimes causes ambiguity. It does so in the present case. The Revenue's argument assumes that its effect is that "employee" means "employee and director", so that, as the Court of Appeal held, a person who is both an employee and a director does not retire unless he retires from both. F G

28. But this is not what the definition says. It says only that the word employee "includes a director." This does not tell us unambiguously what words should be substituted for "employee" wherever that word appears. It may mean that we should substitute the words "employee and director" (in which case the member must retire from both); the words "either as employee or director" (in which case he may retire from either and receive the same benefits as if he had retired from both); or the words "whether as employee or director" (in which case he may retire from either and receive the benefits attributable to the position from which he has retired). H

29. The ambiguity is, however, easy enough to resolve. The recitals to the trust deed explain its purpose as the provision of benefits to "directors and employees" of the company, and this cannot sensibly be confined to persons who are both employees and directors. It must mean persons in the service of the company whether as employees or directors. The underlying concept, therefore, is that of pensionable occupation whether as an employee or director. It follows I

A that the word "retire" means "retire from the service of the company whether as employee or director".

30. It is, therefore, not necessary that a member who is an employee and a director should retire from both positions. Under the terms of the trust deed benefits are related to final remuneration, so that unremunerated service is not B a pensionable occupation. The fact that the taxpayer has remained in his non-pensionable occupation as a non-executive director cannot affect his right to benefit on retiring from his only pensionable occupation. But it would make no difference if he had received and continued to receive director's fees. He would still have retired from his pensionable occupation as an employee, though benefit would have to be calculated without reference to his director's fees.

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31. The definition of "relevant benefits" in the 1970 Act (incorporated into the trust deed by clause 3) distinguishes between "retirement" and a "change in the nature of the service of the employee", though for the purposes of the 1970 Act relevant benefits may properly be paid in either event. The trust deed, however, provides for benefit to be paid only on "retirement". The Court of Appeal held that the effect of incorporating the statutory definition of "relevant D benefits" into the trust deed was that a change in the nature of service does not constitute "retirement" for the purposes of the trust deed. By ceasing to serve as an employee and continuing to serve as a director, it held, the taxpayer had merely changed the nature of his service.

32. I am not at all convinced that the incorporation of the statutory E definition into the trust deed for an entirely different purpose has this effect. But it is not necessary to decide this, for a proper appreciation of the meaning of the word "employee" disposes of the point. What is outside the scope of the word "retirement" in the 1970 Act is a mere "change in the nature of service whether as an employee or a director". This is not what happened. The taxpayer ceased to be an employee altogether.

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33. I reach this conclusion with some satisfaction. The Court of Appeal's ruling would mean that under the trust deed as drawn a member who was an employee and a director and retired from service as both but was reappointed a director on the following day would have "retired" and be entitled to benefit, but a member who like the taxpayer retired from service as an employee but continued in office as a director without remuneration would not; and on finally G retiring from his unpaid office as a director the latter would be entitled to benefit calculated by reference to his final remuneration, (quite possibly nil). These absurdities, moreover, would be the consequence, not of the 1970 Act or of any statutory restriction on benefit, but of the construction of the trust deed placed upon it by the Court of Appeal and the incorporation for a quite different purpose into the trust deed of a statutory definition of relevant benefits.

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Were the payments made out of the trust funds?

34. This makes it unnecessary to express a concluded view on the second question, whether the payments were "made out of" the trust funds if they were paid in breach of trust to a trustee of the scheme in circumstances in which he I came under an obligation enforceable in equity to repay them. It depends on

whether it is sufficient that the payments were made to the recipient for his own use and benefit and were valid to pass the legal title to the money, or whether they must also have been received free from any legal or equitable obligation on the part of the recipient to make restitution. In short, it may depend on whether the determining factor is the payment or the receipt.

Conclusion

35. In my opinion the Commissioner was entitled to find that the taxpayer was both a paid employee and an unpaid director of the company on 30 June 1994. On that finding I am satisfied that on the true construction of the trust deed he retired from service as an employee on that date even though he continued to be an unpaid non-executive director thereafter. If it had been necessary I would also have held that he was eligible to be considered for benefit on early retirement even if he was in ill health as the Commissioner found him to be. It follows that the payments to the taxpayer were duly authorised by the rules of the scheme.

36. I would allow the appeal and discharge the assessments.

Lord Scott of Foscote

My Lords,

37. I have had the advantage of reading in draft the opinions of my noble and learned friends Lord Millett and Lord Walker of Gestingthorpe. Having read the opinion of Lord Millett I had intended simply to express my agreement with his reasons for allowing the appeal. However, having later read the opinion of Lord Walker I find myself persuaded that, for the reasons he has given, Mr. Venables cannot be regarded as having had a contract of service with the company or any of its subsidiaries. Mr. Venables did not, in my opinion, retire from service as an employee, strictly so-called.

38. On the other hand, Mr. Venables did, in my opinion, on the findings of fact made by the Special Commissioner—other than the finding relating to Mr. Venables' "normal health" which was reversed by Lawrence Collins J.—"retire" within the meaning of the pension scheme rules and trust deed. Prior to his "retirement" he had been for 30 years or so an executive director and chairman of the company. He worked about 30 hours a week. During the 15 months prior to his "retirement" on 30 June 1994 he had been the de facto managing director. His workload over this period was about 50 hours a week. It was recorded in the board minutes of 23 June 1994 that he was "retiring as an executive director on 30 June 1994 to pursue other interests but will continue as an unpaid non-executive 'director'". So, after 30 June 1994 he remained an unpaid non-executive director with no work-load or executive responsibilities at all. Why was this not "retirement"?

39. The critical issue, in my opinion, is whether the retention by Mr. Venables of an unpaid non-executive directorship barred him from being treated for the purposes of the pension fund rules and trust deed as having "retired". Under clause 3 of the trust deed, the trust fund is held upon trust to provide:

A "... relevant benefits ... for such employees of the employers who become eligible to participate in the scheme in accordance with the trust deed and the rules."

"Employee" is defined in the trust deed as "a person in the service of the employer and includes a director". Under the rules and the trust deed the trustees B had power "to award an immediate pension to a member who retires in normal health at or after age 50".

40. The Revenue's argument accepted by the Court of Appeal and summarised by Lord Millett at para 24, was that since "employee" was defined as including a director, "retirement" could not take place so long as the individual C remained a director. I, like my noble and learned friend, am unable to accept this reasoning. On the findings of fact in this case, Mr. Venables retired from all the executive responsibilities that he had previously held and on account of which he had received remuneration from the company. If "retire" is given its ordinary meaning as a word in the English language, Mr. Venables retired on 30 June 1994. The definition of "employee" as covering both employees strictly so-called and directors does not, in my opinion, warrant giving the word "retire" or the D concept of "retirement" a narrower meaning than it would ordinarily bear. A managing director, whether formally appointed or de facto, who gives up all his or her executive responsibilities and retains merely an unpaid non-executive office with the company "retires", in my opinion, both as a matter of ordinary language and for the purposes of the rules and trust deed with which your Lordships are concerned in the present case. Save that, in my opinion, Mr. E Venables was not an employee under a contract of service with the company, I am in full agreement with the reasons given by Lord Millett for allowing this appeal.

Lord Walker of Gestingthorpe

F My Lords,

41. Since I have the misfortune to differ from the majority of your Lordships as to the outcome of this appeal I will express my opinion as shortly as possible. It was conceded that the Special Commissioner was incorrect in taking it as common ground that Mr. Venables was an employee of Ven G Holdings Ltd. ("the company") before 30 June 1994. In my opinion the Special Commissioner would also have been wrong in making that finding of fact, since there was no evidence on which he could find that Mr. Venables had a contract of employment (or a contract for services) with the company or any of its subsidiaries.

H 42. It is conceded that there was no written contract. Nor has a search of the company's minutes of board meetings and other records produced any resolution (such as would have been required under para 84 of Table A) authorising the company to enter into a service contract with Mr. Venables. The agreed statement of facts makes no reference whatsoever to a service contract, written or oral. If there had been an oral contract there should have been a I written memorandum of it under s 318 (1)(b) of the Companies Act 1985. There was before the Special Commissioner no evidence as to the amount of the salary

to which Mr. Venables was said to be entitled under any such contract, or otherwise as to its terms. Such material as can be gleaned from the documentary evidence (Mr. Venables's tax return for 1994–95 and the company's unconsolidated financial statements for the years to 30 September 1994 and 30 September 1995) do not support the suggestion that Mr. Venables was until 30 June 1994, entitled to a salary. For 1994–95 Mr. Venables's income from employment was returned as nil (while his dividend income was £77,500). Directors' emoluments were shown in the company's 1994 accounts as: 1993—£25,340; 1994—nil and in the 1995 accounts as: 1994—nil; 1995—£992.

43. The fact is that the affairs of the group seem to have been managed with the high degree of flexibility, and some degree of informality, which often characterises a company or group dominated by a single individual. But it is precisely when a single individual is in a dominant position that proper procedures are most important. Any contract between Mr. Venables and any group company must have raised an obvious conflict of interest (especially as he owned four fifths of the company's shares in a fiduciary capacity) and such a contract could have been properly effected only in accordance with the procedure prescribed by article 84. In practice Mr. Venables seems to have been able to achieve what he wanted without having any service contract. In my opinion the only conclusion open to the Special Commissioner was that his right to emoluments from the company were limited to his rights under articles 82 and 83, which did not depend on an individual contract.

44. My noble and learned friend, Lord Millett (whose opinion I have had the advantage of reading in draft) has referred to the decision of the Court of Appeal in *Secretary of State for Trade and Industry* v. *Bottrill* [2000] 1 All ER 915; [1999] ICR 592. The issue in that case was whether a controlling director could be an employee for the purposes of s 230 of the Employment Rights Act 1996. The director had a written contract of employment which specified his duties, his working hours and his entitlement to remuneration (subject to annual review by his fellow directors). Nevertheless there was an issue as to whether the contract should be taken into account for the purposes of the Employment Rights Act. The case does not in my view assist as to the circumstances in which an oral contract should be inferred.

45. It is common ground that material relevant to the construction of the group pension scheme includes its fiscal context: the tax advantages of approved occupational pension schemes, the statutory provisions as to mandatory and discretionary approval, and (so far as notorious enough to be within the actual or presumed knowledge of the parties) the way in which the Superannuation Funds Office of the Inland Revenue exercised its statutory and managerial discretion at the material time. It was argued that Chadwick L.J. went beyond that in his predisposition to give to an expression not defined in the rules—that is, "retirement" and allied expressions—the same meaning as in Chapter II of Part II of the Finance Act 1970.

46. I respectfully think that Chadwick L.J. was right to start with that predisposition, and that he was also right to conclude that nothing in the trust deed (including its schedules) led to a different conclusion. Although the trust deed was (as your Lordships were told) based on a published precedent, the deed cannot be regarded as well drafted. It would be unsafe to treat any apparent

A nuances in its language as being significant. The safer course is to give "retirement" its normal meaning in the statutory scheme. If the issue had been posed the other way round—that is, if it had been in the Inland Revenue's interest to contend that "retirement" as used in the deed should be given some meaning different from its meaning in the statute—your Lordships would, I venture to think, have been disinclined to hear the argument sympathetically.

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47. In my opinion it follows that Mr. Venables was at all material times, by virtue (and exclusively by virtue) of his directorship of the company, an employee (as defined in the deed) in service (as defined in the deed) and that relationship continued until he ceased to be a director of the company. His retirement must be related to the end of his directorship, since it was the only qualification that C he had for membership of the pension scheme. There was in my opinion no proper ground for treating his informal transition from executive to non-executive directorship as amounting to retirement.

48. Lord Millett has referred to anomalies resulting from the position in which (on the view taken by the Court of Appeal) Mr. Venables would have found himself. I think, with great respect, that the first anomaly tends to overlook (as Mr. D Venables himself may possibly have overlooked) the difficulties arising from Mr. Venables's conflicting interests while he was still an executive director—as the real driving force of the company, as a trustee of the pension scheme, and also as a trustee of the family settlement which held 80 per cent. of the shares in the company. It would not have been right for Mr. Venables, with so many conflicting personal and fiduciary interests, and knowing that he was to be reappointed as a E director the next day, to join in exercising in his own favour the discretion to permit early retirement. Moreover the figures in the tax return and accounts (although admittedly sketchy) suggest that he might in any event have had some difficulties in achieving what he wanted in the way of final remuneration.

49. If (contrary to the view of the majority) Mr. Venables became subject F to a large tax liability, I would feel some sympathy for his position, but that sympathy would be qualified. It was said that Mr. Venables was a practical businessman who could not be expected to deal with the finer points of company law and pensions law. But he had lawyers, accountants and actuaries to give him expert advice. He hoped to obtain, through the company's approved occupational pension scheme, a large tax-free sum which it might have been G difficult for him to obtain in any other way (I was unpersuaded by Mr. McDonnell's submission, skilfully though it was put, as to the marginal attractions of approved pension schemes). It was incumbent on Mr. Venables, in order to obtain those advantages, to ensure that matters were arranged properly. The difficulties arising from his fiduciary obligations (as pension trustee, family trustee and director of the company) were not simply a matter of formality.

H 50. I consider that the Court of Appeal were also correct in their view on s 600 of the Income and Corporation Taxes Act 1988. I would therefore have dismissed this appeal.

[Solicitors:—Messrs. Warner & Richardson; Solicitor of Inland Revenue.]

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