

ENGLAND AND WALES / JUDGMENT

Southgate & Anor v Sutton & Ors

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Neutral Citation Number: [2011] EWCA Civ 637 IN THE COURT OF APPEAL (CIVIL DIVISION) ON APPEAL FROM THE HIGH COURT OF JUSTICE CHANCERY DIVISION THE HON MR JUSTICE MANN HC09C04405 Case No: A3/2010/0658 Royal Courts of Justice Strand, London, WC2A 2LL Date: 26 /5/2011 Before : LORD JUSTICE MUMMERY LADY JUSTICE SMITH and LORD JUSTICE WILSON

- ----- Between : CHRISTOPHER SOUTHGATE & ANOR
- and - PETER SUTTON & ORS Appellants Respondents
- -----
- ----- MR CHRISTOPHER McCALL QC (instructed by Baker & McKenzie LLP) for the Appellants MRS SHAN WARNOCK-SMITH QC (instructed by Charles Russell LLP) for the 1st, 2nd & 3rd Respondents Hearing date: 22nd October 2010
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Judgment

Lord Justice Mummery: The decision 1. 2. The court announced, at the end of the oral hearing, its unanimous decision to allow this appeal. An agreed form of order was approved by the court and it was entered bearing the date of that decision. For reasons well known to the parties there was more urgency in having the order than in knowing the reasons for making it, which are, for my part, stated in this belated judgment. The appeal was about the scope of two provisions in the Trustee Act 1925: s.57(1) under which trustees may apply to the court for the conferral of necessary powers for the purposes of expedient transactions in the management and administration of the trust property; and s.32(1) under which trustees have a power of advancement. The background 3. Trustees facing difficulties in the management or administration of the trust property may be advised that they do not have the necessary legal powers, either under the trust instrument or under the general law, for the purpose of a transaction that is considered to be in the best interests of the beneficiaries. In those circumstances the trustees may apply to the court under s.57(1) of the Trustee Act 1925. If, in the opinion of the court, the proposed transaction is expedient, the court may by order confer on the trustees the necessary powers for that purpose. 4. Section 57(1) provides that:- “Where in the management or administration of any property vested in trustees, any sale, lease, mortgage, surrender, release, or other disposition, or any purchase, investment, acquisition, expenditure,

or other transaction, is in the opinion of the court expedient, but the same cannot be effected by reason of the absence of any power for that purpose vested in the trustees by the trust instrument, if any, or by law, the court may by order confer upon the trustees, either generally or in any particular instance, the necessary power for the purpose, on such terms and subject to such provisions and conditions, if any, as the court may think fit and may direct in what manner any money authorised to be expended, and the costs of any transaction, are to be paid or borne as between capital and income.” 5. 6. On an application under s.57 the court must be satisfied on two main points before it can exercise its discretion to confer the powers requested: first, that the powers sought are for the purpose of a transaction “in the management or administration of any property vested in trustees”; and, secondly, that the transaction is, in the opinion of the court, “expedient,” meaning that it must be in the interests of the trust as a whole. The expressions “other transaction” and “expedient” in s.57(1) are very broad. However, they are confined by the context of the “management or administration” of the trust property. Thus, it has been held that there is no jurisdiction under s.57(1) to confer a power to depart from the beneficial interests under the trusts by re-writing, remoulding or re-arranging them. Variations of the beneficial interests under the trusts 7. 8. 9. 10. are not, as such, matters of “the management or administration” of the trust property and “trust property” cannot be equated with beneficial interests in the trust property. Rulings to that effect in *Re Downshire* [1953] Ch 218 at 248 and *Chapman v. Chapman* [1954] AC 429 led to the passing of the Variation of Trusts Act 1958 (the 1958 Act). That created a new jurisdiction under which the court may, if it thinks fit, approve proposed arrangements varying trusts, including the beneficial interests under them, on behalf of infants, unborn persons and others, if the carrying out of the arrangement would be for their benefit. It has been held, on the other hand, that an application under s.57(1) to confer powers for the purpose of a proposed transaction is within the jurisdiction of the court, if the exercise of the powers conferred by the court under s.57(1) might only incidentally affect the beneficial interests in the trust property: see *Downshire* at 248 per Lord Evershed MR. The court must decide, on the particular facts of each case, on which side of the line the application falls. That may be difficult, especially when, as is the case here, the application is not opposed. The court is nervous about the fundamental matter of jurisdiction if it is asked to act without the benefit of adversarial argument that normally disciplines its decision-making processes. In those circumstances counsel for the concurring parties bear a special responsibility. It is their duty to give the court all the help that it requires to reach the right decision. It must be established to the satisfaction of the court (a) that it has jurisdiction to entertain the application and (b) that it can properly exercise its discretion to do what is being asked of it. In this case the transaction for which trustees seek conferral of powers is one of appropriation and partition of the trust property vested in them. It is common ground that the trustees have no existing power to appropriate or partition the trust property. The powers are sought for the purpose of a transaction creating a sub-trust of separated funds for the benefit of those beneficiaries under a family trust who are resident in the United States (the Southgate Beneficiaries). Along with other beneficiaries resident in the United Kingdom the Southgate Beneficiaries are at present interested in the income and capital of the whole of the trust property. Under the transaction proposed by the trustees in their application the Southgate Beneficiaries will, under a separate

sub-fund to be administered by appointed US trustees, be entitled to beneficial interests in the whole of the income and capital of the trust property appropriated to what will be called “the Southgate Sub-Fund”. 11. It is contended by counsel for the concurring parties that the proposed transaction has only an “incidental impact” on the beneficial interests in the trust property; that it falls within the scope of s.57(1); and that the court ought to exercise its discretion to grant the application.

12. Mann J had no difficulty in satisfying himself that the proposed transaction would be expedient for the trust as a whole, but he declined to grant the application on the ground that he was not satisfied that it fell within the court’s powers under s.57(1). He regarded the effect of the proposed transaction on the beneficial interests in the trust property as rendering them “conceptually different” rather than a change in how the interests are in fact enjoyed. He said that the partition proposed in this case “would create a different set of beneficial interests, qualitatively speaking, to those which currently exist”. The partition and appropriation would vary the beneficial interests in the trust property so that, instead of enjoying a share of the income of the whole fund, the Southgate Beneficiaries would enjoy the income of part of the fund, though the actual income received would be likely to be the same or similar depending on the state of investment. In my view, the judge acted correctly in voicing real concerns about the limits of the court’s jurisdiction. He was also correct in adopting a cautious approach to what he was being asked to do. Understandably he wanted to be as certain as he could be that the court had the necessary jurisdiction to make the orders and that it was a proper case for the exercise of judicial discretion. The careful detailed reasons in his judgment [2009] EWHC 3270 (Ch) raise an issue of practical significance on the scope of the court’s jurisdiction under s.57. In short, Mann J formed the view that the purpose of the proposed transaction was an alteration of the beneficial interests under the trust. He held that such a purpose took the proposed appropriation and partition transaction out of the scope of what he could properly approve under s.57(1) and possibly into the realm of the 1958 Act and its statutory jurisdiction to approve variations in the beneficial interests. No application under the 1958 Act was before the court. 13. 14.
15. Mann J went on to decline the order sought on the second part of the application for a declaration that the trustees are at liberty to exercise the power of advancement under s. 32 of the 1925 Act. The trustees’ proposal before him involved the advancement of cross-accruer rights in the trust property. He held that the proposal contained in a resolution of the trustees excluding contingent interests in the trust property was outside the section: it was not a dealing with the trust property vested in the trustees, but was rather a variation of the beneficial interests under the trusts. At the hearing in this court the force of what Mann J said was recognised and permission was sought from and granted by this court to replace the original proposal with a re-draft of the trustees’ resolution for the proposed exercise of the power of advancement. The appeal

16. Mann J granted permission to the Southgate Beneficiaries to appeal on both aspects of his order dated 2 March 2010. 17. The Southgate Beneficiaries are supported by the respondent trustees (the Trustees) of Trust Deeds dated 1 October 1940 and 4 November 1940 (the Settlement) made between Arthur C England and JW England and others. Mr Christopher McCall QC appears for the Southgate Beneficiaries. The Trustees of the Settlement, for whom Mrs Shan Warnock-Smith QC appears, were the claimants seeking the additional powers and authorisations for appropriations and advances. The remaining respondents played no part in the appeal. The Settlement and the proposal 18. The details of the Settlement are set out in the judgment of Mann J, who was also asked to deal with a range of other matters. Most of them are irrelevant to this appeal and need not be repeated. 19. 20. The Settlement was made by four brothers. An outline of its terms will suffice. They are that, on the death of the last surviving issue of the settlors living at the date of the Settlement, the fund is to be divided between the issue per stirpes, each of the settlors being head of one of the stirps. Until the death of the last surviving issue the income was to be paid to the settlors until their deaths and thereafter to their children with successive generations taking, if prior generations failed. There are cross-accruer provisions within each stirps and in favour of other stirpes if any stirps fail. Some of the beneficiaries have assigned their interests to companies. The residence of the Southgate Beneficiaries in the United States is the source of the difficulties faced by the Trustees in the administration of the trust property. The problems arise from the combined effect of UK and US tax provisions. The proposal to partition the trust property and to make an advancement by way of re-settlement is structured in such a way as to avoid the potentially disastrous tax consequences for the Southgate Beneficiaries of leaving things as they are. The proposed appropriation and partition to form the Southgate Sub-Fund will avoid UK tax and reduce US tax. The advancement, now proposed to be done by way of re-settlement extinguishing cross-accruer interests under the Settlement, would reduce the tax liabilities of the Southgate Beneficiaries further, so that the Southgate Sub-Fund would fall within Schedule 4ZA to the Taxation of Capital Gains Act 1992 and no person would be a beneficiary both under that Sub-Fund and the principal trusts of the Settlement. The cross-accruer provisions of the Settlement created a potential for cross-interests and thus for the Southgate Beneficiaries to include persons interested to have a beneficial interest in each of two separate funds. The exercise of the power of advancement is proposed in order to exclude that possibility and its consequential fiscal cost in inheritance tax and capital gains tax. Fresh evidence 21. 22. 23. 24. Before turning to the judgment of Mann J and the submissions about it, I should refer to the fresh evidence adduced in this court pursuant to permission granted by it. Mann J would have been assisted by this evidence, if it had been put before him at the original hearing. The evidence related first to the up-to-date position as to the importance to the Southgate Beneficiaries of having US trustees of the Southgate Sub-Fund as their prospective share of the settled property, having regard to (1) the increase in the rate of capital gains tax from 18% to 28% to which the trustees of an English trust are exposed and (2) the recent high degree of volatility in the dollar/sterling exchange rate. These matters are relied on by the parties as indicating a real possibility that the entire capital share of the Southgate

Beneficiaries would otherwise be swallowed up by avoidable burdens of double taxation. It was explained that it would be desirable, if possible, to implement the proposed split of the funds before 31 December 2010, that being the end of the US tax year. Hence the urgency in the court reaching a decision at, or soon after, the hearing, even though reasoned judgments remained to be given at a later date. Secondly, the fresh evidence shows that (1) it would not appear to be possible to obtain the agreement of all the adult beneficiaries resident in the UK to an application under the 1958 Act to approve an arrangement; (2) the s.57 jurisdiction appears to be the only way open to the trustees by which they can achieve a separation of a beneficiary class consisting of two groups of beneficiaries; and (3) there is a serious and deepening rift between the beneficiaries, such as to make the task of the trustees in holding an even hand between them more difficult than had been assumed when the matter was before the judge. The problem was that an administration of the trust property that suited one branch of the family did not suit the other branch. So it was contended that the best interests of the beneficiaries as a whole would be served by creating a sub-trust for the Southgate Beneficiaries in respect of their interests in income and capital. The trusts would remain the same, the change being in the asset from which the income is derived. Thirdly, there is now available material which was not before the judge explaining the factual background to the case of *MEP v. Rothschild Trust Cayman Limited* (Cause Nos 128 of 2009 and 576 of 2005), a decision of the Grand Court of the Cayman Islands (The Hon Anthony Smellie, Chief Justice) on 20 October 2009 that was cited to Mann J as a decision on the statutory provisions in the Cayman Islands equivalent to s. 57. The judge referred to the case and distinguished it. It had not been fully reported. The new material is relied on to show that that case, in which very experienced English trust counsel persuaded the Cayman Chief Justice to make an order under the local equivalent of s.57, is almost identical to the present case in relevant respects. Fourthly, regarding the power of advancement, counsel and those whom they represent have taken account of the comments of Mann J in his judgment that he could not approve the proposal before him, as it was in the form of a draft resolution relating to the beneficial interests rather than to the capital of the trust fund. In the light of the judge's comments the Trustees have produced a re-structured resolution to be scheduled to the order of the court. In brief, it is to the effect that, by way of application of the capital comprised in the Settlement for the benefit of the beneficiaries Christopher Southgate and Richard Southgate, the same shall henceforth go and be held on the like trusts as are applicable thereto, subject only to variations as to the trusts applicable to certain contingent reversionary interests of Christopher and Richard Southgate. 25. 26.

27. With that additional material in mind I turn to consider the two aspects of the application rejected by the judge. A. Appropriation/partition point The judgment 28. 29. The submissions in this court concentrated on the judge's consideration of the authorities and the conclusions reached by him about their effect on the construction of s.57(1) and its application to this case. The judge was influenced (over-influenced, say Leading Counsel for the parties) by dicta in the judgment of Goff LJ in this court in *Re Freeston's Charity* [1978] 1 WLR 741 (Freeston). Central to the decision in that case was a distinction drawn between

- (a) a trust in which the beneficiaries have specified interests in the whole of the fund and (b) a trust in which they have an interest in the whole of the specified portion of a fund. Mann J relied on that distinction in concluding that an appropriation of the part of corpus of the Settlement fund to the Southgate Sub-Fund, in which the Southgate Beneficiaries would henceforth have their beneficial interests, would be a variation of the beneficial interests falling outside the court's powers under s.57(1). 30. The case of *Re Thomas* [1930] 1 Ch 194 was cited to the judge as an instance of the court conferring a power of partition under s.57(1). Farwell J said at p.198:- "This therefore being a case where partition cannot be effected under any power vested in the trustees by the trust instrument or by law, I am entitled to consider whether it is expedient and ought to be carried into effect. If so I can authorise the trustees to effect it under the Trustee Act, 1925, s.57, provided that I am satisfied that it cannot be effected in any other way..."
31. Mann J observed that in *Thomas* the order was made in circumstances in which the trusts already gave interests of portions of a fund to various classes of beneficiaries and the interests were to be substituted by interests in parts of the divided fund. 32. 33. In the case of *MEP v. Rothschild Trust Cayman Ltd* appropriations to a sub-trust for administrative reasons were approved under the local equivalent of s. 57. Mann J distinguished that case as one in which the trusts affecting the funds in the sub-trusts were precisely the same as they were before the appropriation. In this case the judge said that the whole point of the partition proposal was to create trusts of divided shares in place of trusts of income over a whole undivided fund. The partition would, he said, create "a different set of beneficial interests, qualitatively speaking, to those which currently exist." It was not a case of just an "incidental" effect on the beneficial interests. In holding that the proposed power of appropriation and its proposed exercise were outside the scope of s.57(1) the judge said that he did so with a little regret because, in terms of expediency, the case would have been made out. His regret was tempered by the fact the same result could be achieved by a variation of the trusts with an application under the 1958 Act, though it had been hinted to him that such might not be possible. Discussion and conclusions on appropriation/partition 34. For the Southgate Beneficiaries, and supported by Mrs Shan Warnock-Smith QC for the Trustees, Mr Christopher McCall QC contended that the judge reached the wrong decision on the application of s.57(1), because he had approached the proposal from the wrong point of view. He should have asked whether the Trustees had a problem in the management or administration of the trust property and whether, for its solution, they needed to have the power of appropriation sought. They clearly face problems in the administration of the trust property. There was no valid objection to the solution proposed, because the effect on the beneficial interests is incidental only. Instead, Mr McCall submitted, the judge wrongly characterised the proposal as for the alteration of the beneficial interests and as a conceptual change rather than as a change in how the interests are in fact enjoyed. 35. On this aspect of the case the court decided to allow the appeal. My reasons for having subscribed to the order are as follows. 36. 37. 38. 39. 40. First, as already explained, I am entirely with the judge in adopting a cautious approach to the jurisdiction invoked under

s.57(1). Secondly, there is no binding authority which required the judge to reach the decision that he did. In Freeston, on which the judge particularly relied, this court affirmed the judgment of Fox J. Its ratio is binding on us. Although it was not a decision on s.57(1) (and so Downshire was not even cited) and the observations on its scope are therefore obiter, Freeston has potential relevance to this case in its recognition that (a) there is a distinction between a dealing with the trust property and a variation in the beneficial interests in it; and (2) there may be a variation in a beneficial interest in trust property, if the trust fund is partitioned so that a beneficial interest in the whole fund ceases and is replaced by a beneficial interest in a partitioned part of the fund. In my judgment, however, the circumstances in Freeston were very unusual and far removed from the circumstances of this case. The trust in Freeston was a perpetual gift dating from 1597 of equal shares of income to two charities. One of the charities was University College, Oxford, which was also the sole trustee. The trusts never envisaged an ultimate split of capital and, if the capital had been split, that change would have had more than an incidental impact on the beneficial interests. The trust fund was divided under a scheme at a certain time and in such a way as to affect the beneficial interests of the object of the charity. The issue was whether the division of the funds had been properly made, or was a breach of trust which should be remedied. The reasons for the division of the trust fund had nothing to do with the purposes for which power to deal with the trust property may be conferred under s.57 (1). As Fox J said at first instance [1978] 1 WLR 120 at 127-8 the appropriation was not “mere administration” but was an alteration of the beneficial interests and he added at 128A:- “The right to one moiety of the income of a fund is quite a different thing from the right to the income of a severed moiety of the fund. And the difference is not just a technicality. The advantages from the point of view of investment and administration in keeping a large fund intact may be substantial.” The reference to s. 57(1) only arose from the submission of counsel for the College that the partition of the fund could have been authorised under it, a submission that was rejected by the court. It was in that context that Goff LJ said at p751-2 that s. 57(1) does not enable the court to vary the beneficial trusts, having observed that that:- “...it is manifest that an interest in half the income of an undivided fund is quite different from the whole income of a divided half of that fund.” In my judgment, Freeston is distinguishable. It is not authority for an unqualified proposition that the partition of a trust fund is always a variation or re-arrangement of the beneficial interests in it, or always has more than an incidental impact on the beneficial interests in it. Freeston was a case of altering the nature of the beneficial interests by the division of the fund, but in circumstances where there were no difficulties “in the management or administration of the trust property.” Nor was there any suggestion of expediency which would have justified the conferral by the court of a power to partition the trust property. There was no difficulty of the kind present here of the Trustees having to act even-handedly and having to reconcile the different interests of the different beneficiaries under the Settlement. The judge was unable to derive much assistance from what he was shown about the Cayman case of Rothschild. The judgment, which has not been reported and is not binding, is entitled to judicial respect. As a result of the grant of permission to adduce further evidence this court

has been shown, but Mann J was not, a letter explaining the facts in that case. They were practically identical to those in this case. Smellie CJ reasoned that, although the partition would alter the structure of the trust, the sub-trusts remained governed by the terms of the original trust and were unaltered. There was only an incidental impact on the respective beneficial interests. That case was therefore an instance of the creation of the partitioned sub-trust, which anticipated the ultimate division of capital, being achieved by an application under a similar jurisdiction to that under s.57(1). There was an incidental change in the nature of the beneficial interests, but no change in the type of beneficial interests enjoyed under the terms of the original trust.

42. Mann J was not put as fully in the picture as was this court about the prospects of an application under the 1958 Act. Without prejudice to his submission that this is a case of an administrative trust problem properly dealt with under s. 57(1), Mr McCall QC relied on the fresh evidence to show the difficulty in obtaining the consent of the beneficiaries for the purposes of an application under the 1958 Act. 43. In conclusion, I was in favour of this appeal being allowed, as I was satisfied by the submissions of Leading Counsel on the law and by the evidence in this case that the court had jurisdiction to grant the application as one relating to the administration of the trust property; that the impact of the proposal on the beneficial interests was incidental only; that there was no legal precedent or other obstacle to granting the application and making the order asked; and that the proposed transaction for appropriation and partition was one that was clearly expedient in the interests of the trust as a whole and was the only way in which the benefits of the separation of the interests of the Southgate Beneficiaries could be achieved. B. Advancement point 44. The power of advancement contained in s. 32 of the 1925 Act provides that:- “(1) Trustees may at any time or times pay or apply any capital money subject to a trust, for the advancement or benefit, in such manner as they, in their absolute discretion, think fit, of any person entitled to the capital of the trust property or of any share thereof, whether absolutely or contingently on his attaining a specified age or on the occurrence of any other event, and whether in possession or in remainder or reversion, and such payment or application may be made notwithstanding that the interest of such person is liable to be defeated by the exercise of a power of appointment or revocation, or to be diminished by the increase of the class to which he belongs: Provided that- 45. 46. 47. 48.
- (a) the money so paid or applied for the advancement or benefit of any person shall not exceed altogether in amount one-half of the presumptive or vested share or interest of that person in the trust property; ... The judge declined to make an order relating to the advancement proposed to him in the form of a draft resolution of the trustees that the relevant beneficial interests should be absolute and free from any contingency. He declined on the ground that s.32 permitted the advancement of trust property in the form of capital money subject to the trust. What was proposed here was to advance a contingent interest under the trust rather than to advance property subject to the trust. It was a variation of the trusts to exclude the contingent interests, not an application of capital under s32. The judge said:- “50. ...Thus a distinction is drawn between an interest in the trust property on the one hand , and the trust

property itself on the other. An advancement under the section deals with the latter. The proposal of the trustees deals with the former. What they are proposing is a variation of the trusts to exclude contingent interests, not the application of 'capital money [property] subject to a trust'. " In this court the form of the advancement proposed has been restructured to take account of the point made by the judge and to bring what is proposed within the scope of *Pilkington v. IRC* [1964] AC 612. That case was cited to this court for the proposition that, in appropriate circumstances, an advancement may be by way of re-settlement of the trust property varying only the trusts applicable to part only of the beneficial interests in the trust property. That is what is now proposed in relation to the elimination of the cross-accruers from the re-settlement. *Pilkington* was not cited to the judge. The judge made a valid point in drawing attention to the distinction between the advancement of property subject to the trust and an interest in the trust property. That distinction was reflected in the re-structuring of the proposed form of the advancement put before this court in the form of a fresh draft resolution of the Trustees which, it was submitted and I accept, would be a valid exercise of the power of advancement under s. 32. There was attached to the order of the court the draft resolution of the advancement of the Trustees relied on by Mr McCall QC during the course of the oral hearing of the appeal and later exhibited to a witness statement of Mr Robert Blower, solicitor to the Trustees, dated 26 October

2010. The fresh resolution replaced the draft resolution which Mann J declined to approve.

According to the replacement resolution, the Trustees are of opinion that to exercise their powers under s.32 as to certain parts of the presumptive entitlements of Christopher Southgate and Richard Southgate under the Settlement would be for their respective benefit and would not exceed the limits imposed by proviso (a) to section

(1) of s. 32. In exercise of the powers the Trustees thereupon resolve by way of application of the capital comprised in the Settlement for the benefit of Christopher and Richard the same should henceforth go and be held on the like trusts as are presently applicable thereto subject only to variations as to the trusts applicable to certain contingent reversionary interests of Christopher and Richard, which are then set out, so that their respective entitlements should be absolute and beneficial entitlements free from all contingencies but subject thereto preserving all other entitlements of Christopher and Richard and of any other person interested under the Settlement including in particular all interests taking effect in priority to the said contingent reversionary interests. Result 49. As requested and as mentioned above, counsel agreed a draft order for the consideration of the court and the Trustees put in evidence the re-draft of the advancement proposal handed to the court by Mr McCall QC in the course of the appeal hearing. The court order has been dated and entered to reflect the consequences of allowing the appeal on both points. Lady Justice Smith 50. I agree. Lord Justice Wilson

51. My reasons for having subscribed to the order which was made on the appeal are identical to those set out by Lord Justice Mummery.

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