One of the great advantages of a trust is its flexibility. It is usual to draft trusts with as much flexibility as possible giving trustees wide overriding dispositive powers.

Sometimes, particularly in the case of older trusts, that flexibility is missing in which case it may be necessary to apply to court for help.

I. EXERCISING DISPOSITIVE POWERS

Most settlements have two separate dispositive powers: (1) a power to appoint income and capital, and (2) a power to apply income and capital for the advancement or benefit of beneficiaries. There is also usually a power to appropriate which can be regarded as semi-dispositive. These powers allow the terms of the trust to be extensively modified.

1.1 A power of appointment.

The following is a typical power of appointment:

“

My Trustees (being at least two in number or a trust corporation) may at any time or times:

(i) by deed or deeds revocable (during the Trust Period) or irrevocable appoint that all or any part or parts of the income or capital of my Trust Fund shall be held on such trusts (including discretionary and protective ones) in favour or for the benefit of all or any one or more of the Beneficiaries and with and subject to such powers (including dispositive and administrative ones exercisable by my Trustees or any other person) and other provisions as my Trustees think fit"

These powers enable the original trusts of the settlement to be modified. Trustees are likely to use this power when they want to keep property within the trust but want to vary the terms on which it is held, for example changing an age contingency.

In general, a power of appointment cannot be used to transfer funds out of the settlement freed from the original trusts (because this is not a modification of the existing settlement). However, some powers expressly authorise this.

In Bond v Pickford [1983] STC 517, the court distinguished two types of power: a power in the narrow form (modifying the existing trusts) and a power in the wider form (allowing a transfer out of the settlement). However, even a power to transfer property out of the settlement will not authorise the trustees to transfer on new discretionary trusts, unless clear words have been used because of the principle of delegatus non potest delegare.

It is important to know whether or not the exercise of a power of appointment (or power of advancement) creates a new settlement. The creation of a new settlement...
settlement will have CGT consequences because there will be a deemed disposal when the trustees of the new settlement become absolutely entitled as against the trustees of the original settlement (albeit that they may be the same persons). Entitlement does not need to be beneficial to create a deemed disposal. A line of CGT cases has explored when a ‘new’ settlement arises.

In *Roome v Edwards* [1982] AC 279 Lord Wilberforce drew a distinction between trustees using a special power of appointment to modify the existing trusts of a settlement (no new settlement) and the exercise of a wider form of power where property is removed from the original settlement and subjected to other trusts (resettlement). He identified the following indicia to decide whether a new settlement had been created:

(a) separate and defined property;

(b) separate trusts;

(c) the appointment of separate trustees;

(d) a separate disposition bringing the separate settlement into existence.

The approach of Lord Wilberforce was refined and developed in *Bond v Pickford* [1983] STC 517 where Slade LJ stressed that the exercise of a power of appointment or advancement cannot create a new settlement unless the trustees have express or implied authority to remove assets altogether from the trusts of the original settlement and bring them within the trusts of a different settlement. It is only where they have this authority that the trustees can free themselves completely from responsibility (in their capacity as trustees of the original settlement) for the property appointed or advanced.

In *Swires v Renton* [1991] STC 490 Hoffmann J (as he then was) made the important point that where a settlement contains a special power of appointment drawn in the wider form, trustees do not have to use it to take the assets out of the settlement; they could choose to use it in a narrower way keeping the property within the settlement and simply modifying the trusts on which it is held.

The consequence of these decisions is that when drafting settlements, a selection of powers should be included so that trustees are free to transfer property out of the settlement onto whatever kind of trusts they wish but can also use narrower powers to modify the existing trusts.

Power to transfer to new settlement

“*My Trustees (being at least two in number or a trust corporation) may at any time or times:

(ii) transfer all or any part or parts of the income or capital of my Trust Fund to the trustees of any Settlement or Will Trust*
wherever established (whose receipt shall be good discharge to
them) to be held free from the trusts of my Will and on the trusts
and with and subject to the powers and provisions of that
Settlement [but only if those trusts powers and provisions are
such that (at the time of the transfer) they could themselves
have created them under (i) above]”

When exercising the powers given to them trustees should indicate the way in
which they are exercising their powers: for instance ‘by way of resettlement’ or
‘in modification of the existing trusts’.

It is important to comply with any formalities required by the trust instrument.
Failure to do so will render the purported action void. Normally the trust
instrument requires a power of appointment to be exercised by deed. In Pitt v
Holt; Futter v HMRC [2013] UKSC 26 Lord Walker agreed with the Court of
Appeal that the circumstances in which trustees’ actions can be set aside are
limited to cases of:

- excessive execution that is something that goes beyond the scope of
  the power such as a procedural defect, including the use of the wrong
  kind of document - what is ‘done’ is void;

- inadequate deliberation on the part of the trustees which is sufficiently
  serious as to amount to a breach of fiduciary duty – the action is
  voidable at the instance of the beneficiaries.

Common examples of procedural defects are failing to get consent of a
named individual where the trust instrument requires it or failing to use a
deed.

A typical use of a power of appointment is to give a beneficiary a right to
receive income. This is beneficial from an income tax point of view as it
means that the income is no longer liable to the trust rate of income tax but
will be taxed at the beneficiary’s rates. There is still an income tax
disadvantage to passing dividends through a trust without an interest in
possession. The trustees pay tax at 38.1%. If they pay income to beneficiaries
it is treated as ‘trust’ income not ‘dividend’ income and the beneficiary
receives a tax credit of 45%. The trustees are then required to pay the
shortfall (Income Tax Act 2007, s496). Effectively the benefit of the lower
dividend rate is lost.

It is therefore beneficial for trustees of trusts without an interest in possession
to exercise their powers under the trust to give one or more beneficiaries a
right to income.

(a) Since the changes to trusts in 2006 conferring a right to income has no
IHT implications unless the trust is a will trust and the appointment is
made within 2 years of death in which case it will be read back into the
will for IHT purposes and will create an immediate post-death interest.
(b) The appointment should be either for a fixed term or be expressed to be revocable. The default possession for appointments is that they are irrevocable unless the contrary is stated.

See Appendix 1.

1.2 A power to apply capital (an advancement-type power).

“My Trustees (being at least two in number or a trust corporation) may at any time or times:

(iii) pay transfer or apply the whole or any part or parts of the capital of my trust Fund for any purpose whatever which the Trustees may think to be for the advancement or benefit of any one or more of the Beneficiaries for the time being in existence

Trustees are likely to use this power when they are giving beneficiaries an absolute entitlement to trust assets, although it is used increasingly to resettle property on different trusts. This power is based on the statutory power of advancement contained in Trustee Act 1925, s 32.

No specific formalities are laid down for the exercise of the statutory power and express powers do not usually require any. A simple trustee resolution will suffice. However, it is important to have a written record of when the advance is made, for example in case of changes in tax rates. The best course is for trustees to resolve that “from this date we are holding [cash/assets] on trust for [Beneficiary] absolutely”

What do the words “advancement or benefit” mean?

According to Lord Radcliffe in Pilkington v IRC [1964] AC 612 the word "advancement" originally meant the establishment in life of the beneficiary who was the object of the power. In the nineteenth century this meant buying an apprenticeship or the purchase of a commission in the army or an interest in business. In the case of women there could be advancement on marriage. Advancement was thought to have a limited range of meaning since it conveyed the idea of some step in life of permanent significance.

It, therefore, became common for those drafting trusts to add words such as "or otherwise for his or her benefit". It was always recognised that these added words were "large words" (see Jessel MR in Re Breeds' Will 1 Ch D 2261).

In Pilkington, Lord Radcliffe said the expression "advancement or benefit" meant "any use of the money which will improve the material situation of the beneficiary". He also said that the word "advancement" does not carry with it the idea of paying money to a beneficiary early. This is often the result since

---

1 See also Jessel MR in Lowther v Bentinck [1874-75] LR 19 Eq 166 where he said that preferment and advancement were "both large words" but that "benefit" was the "largest of all."
the funds advanced come from property in which the beneficiary does not yet have an absolute entitlement but in some cases, such as settled advances, the advancement might actually defer the vesting of the beneficiary’s absolute title.

The use of the words “material situation” in Pilkington might suggest a limitation. In Re Clore, however, Pennycuick J held that:

(a) the improvement of the material situation of the beneficiary is not confined to his direct financial situation but can include the discharge of moral or social obligations particularly in relation to provision for family and dependants (this can be useful in relation to settlements which have not been flexibly drafted and which have a narrow range of beneficiaries);

(b) that the court has always recognised that a wealthy person has a moral obligation to make appropriate charitable donations

**Examples of Benefit**

(1) Payments for maintenance *Re Breeds Will* (1875) 1 Ch D 226.

(2) Discharge of debts *Lowther v Bentinck* (1874) LR 19 Eq 166.

(3) Loan for setting up beneficiary’s husband in business *Re Kershaw’s Trusts* (1868) LR 6 Eq 322.

(4) Making settlements on beneficiaries in no particular need to save estate duty *Re Ropner’s Settlement Trust* [1956] 1 WLR 902; *Re C L* [1969] 1 Ch 587.


(6) A settlement on the beneficiary’s children was held to be for his “benefit” as it relieved him of the "considerable obligation in respect of making provision for their future" which he would otherwise have owed *Re Hampden’s Settlement Trusts* [2001] WLRT 195

*Hampden’s Settlement Trusts* contains the following useful summary of the decided cases:

- a power to apply capital for the benefit of somebody is the widest possible formulation of such power;

- under such a power trustees can deal with capital in any way, if:
  - viewed objectively, it can fairly be regarded as being to the benefit of the object of the power, and
  - subjectively, they believe it to be so;
- such benefit need not consist of a direct financial advantage to the person who is being benefited. It may be that he is benefited by provision for a near relation or by relieving him of moral responsibilities.

2. Power of Appropriation

It is usual to include such a power amongst the administrative provisions.

“Power from time to time to set such a value upon any investments or other property forming part of the Trust Fund as the Trustees shall think fit and to appropriate if they shall think fit any such investments or property at such value in or towards satisfaction of any share or interest under the trusts affecting the same.”

Such a power is often used to allocate assets to particular beneficiaries so as to facilitate accounting. For example a trust fund is settled on four minor grandchildren contingent on them reaching 25. The trustees expect to apply income and advance capital to the grandchildren during the life of the trust. It may make life easier if they allocate the assets into four ‘shares’. In the case of large family trusts particular investments may be particularly suitable for one beneficiary. Another reason for appropriating may arise where different lines of the family are resident in different tax jurisdictions making it necessary for the trustees to pursue different investment policies.

However, often things change and the trustees may want to switch the assets back. When they make the original appropriation, they should expressly reserve a power to re-appropriate.

“We being the trustees of [ ] Will Trust hereby exercise the power of appropriation conferred on us by clause [ ] of the Will to appropriate the assets set out in the Schedule to the fund which is specified in that Schedule and pending transfer of the assets we will hold them on bare trust for the relevant fund PROVIDED ALWAYS that we retain the power in the future to exchange assets appropriated to one fund for assets (or an interest in assets) appropriated to another fund, or which remain unappropriated, which have an equivalent open market value.”

When using the power to appropriate in this way, the separate funds remain under the single trust ‘umbrella’ so there is no deemed disposal and risk of CGT liability.

However, because the funds are within a single trust, a single tax return has to be made dealing with all the funds. Sometimes family members are on bad terms and do not want the information to be shared. In such cases a sub-fund election can be made (provided the proper requirements are met) to treat one or more of the funds as a separate trust for CGT and income tax purposes. It is necessary to
weigh up the importance of confidentiality to the beneficiaries as compared to the possible CGT liability that may be triggered\(^2\).

\(^2\) The sub-fund election has no IHT implications so the trust remains one entity for IHT.
II. AMENDING TRUSTS WHERE POWERS DEFECTIVE

1. Power to add Administrative Powers

A sensible addition to the administrative provisions of the settlement is a clause allowing trustees to give themselves further powers should these be necessary. For example:

**Administrative Provisions**

*If in the administration of the Trust Fund any transaction is in the opinion of the Trustees expedient but the same cannot be effected by reason of the absence of any sufficient power for that purpose conferred by this deed or by law (or by any earlier exercise of the present power) then the Trustees may by deed confer upon themselves either generally or for the purpose of any particular transaction or transactions the necessary power and from the execution of such a deed the Trustees shall have such power as if it had been conferred by this deed.*

In the absence of such a power, it is necessary to apply to court.

2. Trustee Act 1925, s57

2.1 The Section

This allows the court to grant additional powers of management and administration if it is “expedient” to do so. The purpose of the section is to secure that trust property is managed as advantageously as possible in the interests of the beneficiaries. It provides as follows.

“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.”

Applications under s57 are normally made in Chambers on the application of trustees. They are relatively cheap and straightforward.

BUT only powers concerning the management or administration of trust property can be conferred. The court will not make an order if the effect would be to vary beneficial interests. Instead the adult, capable beneficiaries must consent under the rule in *Saunders v Vautier* and an application to court
under the Variation of Trusts Act 1958 must be made on behalf of beneficiaries who cannot consent.

It always used to be said, on the authority of *Re Freeston’s Charity* [1978] 1 WLR 741 that a partitioning of a trust fund varied beneficial interests, and so was inappropriate for a s57 application.

However that case was not actually a s57 application. It was an application to have a purported partitioning of a trust fund into two separate trusts declared ineffective. The two halves of the trust fund had been invested differently: one half in equities and one half in fixed interest securities. The income from the equities half was substantially higher. The judge held that the division and appropriation was an alteration of the beneficial interests: “an interest in half the income of an undivided trust fund is not the same as an interest in the whole income of a divided half of that fund”.

The trustees had no power under the legislation applying to the charitable trust to vary beneficial interests. Hence each beneficiary continued to be entitled to half the income from both portions of the fund.

In *Southgate v Sutton* [2011] EWCA Civ 637 an application for partition was made under s57 and the Court of Appeal accepted that the partition of a trust fund is not always a variation or re-arrangement of the beneficial interests in it, nor will it always have a substantial impact on the beneficial interests in it.

On the facts (some beneficiaries were subject to both US and UK tax and the beneficiaries had such conflicting needs that the trustees found it impossible to deal even handedly with them) the proposed appropriation and partition was allowed as being clearly expedient and in the interest of the trust as a whole.

### 2.2 Examples of applications under Trustee Act 1925, s57

- **Re Portman Estate** [2015] EWHC 536 (Ch): The court granted a power to trade and power for trustees and nominees to charge as this would facilitate good management. A power allowing the trustees to confer on themselves further powers of management or administration was refused on the basis that it would be removing the trust from the supervision of the court and such a power was not generally included as standard.

- **Anker-Petersen v Anker-Petersen** [2000] WTLR 581: Extensions to the powers of investment were allowed.

- **Alexander v Alexander** [2011] EWHC 2721 (Ch): The court gave trustees a power to sell a cottage which had been left to a mother for life remainder to her children. The trust expressly stated that the cottage was not to be sold but it was falling into dereliction and there were no funds to repair it. In the alternative the trustees asked the court to use its powers under the Variation of Trust Act but the court said this was
unnecessary as the application did not involve any alteration of the beneficial interests.

3. Applications under Variation of Trusts Act 1958

3.1 Requirements

The rule in *Saunders v Vautier* allows beneficiaries who are of full age and capacity and between them entitled to the whole beneficial interest to vary the beneficial interests by agreement. Where, as is usually the case, there are minor, unborn or unascertained beneficiaries such agreement cannot be obtained. However, the Court can consent on behalf of such beneficiaries provided it is satisfied that the variation is for their benefit.

The application can only be made if the adult beneficiaries with capacity consent to the proposed change.

Since April 2015 Masters have had jurisdiction to make Variation of Trust Act orders and all claims in the first instance come before a Master. Whether a particular application is more suitably dealt with by a judge is decided on a case by case basis taking account of the complexity and scope of the application, whether there are novel legal issues, the parties involved and the parties’ wishes.

The application is normally made in open court.

In *V v T* [2014] EWHC 3432 (Ch) the applicants asked for the hearing to be in private. The trusts in relation to which the application was made owned shares in a private company and the applicants feared that a hearing in open court would lead to the company’s customers becoming aware of the levels of profit made by the company which would lead to those customers squeezing the profit margins of the company and damaging the value of the trust assets. They further submitted that a hearing in open court would lead to disclosure of the high value of the trust assets and of the identity of the minor beneficiaries which would pose a risk to their personal security and possibly lead to them being targeted and taken advantage of by false friends.

Morgan J refused to allow a private hearing but did impose reporting restrictions.

It was settled law that the public are entitled to attend court proceedings to see what is going on. The media has the right to report court proceedings to the public. The fact that a hearing in open court might be painful, humiliating and a deterrent either to a party or to a witness is not normally a proper basis for departing from the open justice principle. The interest protected by the open justice principle is the public interest in the administration of justice rather than the private welfare of those involved in court proceedings.
The evidence put forward in support of the submission in respect of the disclosure of company profit and the threat to the minors' security was not particularly strong and had not come anywhere near satisfying the requirement of clear and cogent evidence justifying derogation from the open justice principle. However, appropriate steps should be taken to protect the children from the adverse effect on their upbringing and personal development which might well result from an open court hearing generating publicity as to their potential wealth.

Following that case a Practice Note “Variation of Trusts” was issued on 9 February 2017. It states that requests for confidentiality should be made at the preliminary hearing before a Master.

“If the Master is satisfied, based on the evidence, that there is a real prospect of the court being willing to direct that the main hearing should be in private and/or there should be reporting restrictions and/or access to the court file should be limited and/or the proceedings are anonymised then interim orders can be made to preserve confidentiality. An example of such an order is at Appendix A, and is available on the justice.gov website, numbered CH43.

Whether it is appropriate to make an interim order to restrict access to the claim form and evidence on the court file and to make the proceedings anonymous pending the disposal hearing will depend on the circumstances in each case. These orders are not automatic and the applicants will have to provide evidence which justifies the making of such an order.”

The court will require separate representation for the different classes of beneficiaries. See Wright v Gater [2011] EWHC 2881 (Ch) where the court was very grumpy about the fact that there was no separate representation, although it did not actually throw the application out without hearing.

Such applications are therefore more expensive than those made under s57. In Pemberton v Pemberton [2016] EWHC 2345 (Ch) referred to below there were three very eminent QCs involved plus two juniors. For a very ingenious solution to this problem see A v Band [2016] EWHC 340 (Ch) where there were various classes of beneficiaries. Some of the beneficiaries were ‘secondary’ beneficiaries who could become present beneficiaries by appropriate exercises of available powers by the trustees. It was clear that the trustees would only use those powers in the event of some family catastrophe wiping out the ‘primary’ beneficiaries. The trustees used their powers to exclude the secondary beneficiaries for the duration of the application. This removed the need for separate representation at the Variation of Trusts application for persons who were unlikely ever to benefit. Warren J said: “I did not see the method of dispensing with the need for representation of the wider class as other than fully effective, as well as being a sensible and practical approach to the application”.

11
Applications under the Variation of Trusts Act can only be made to vary existing trusts not to resettle the trust property by substituting entirely different trusts.

In *Re T's Settlement Trusts* [1964] Ch 158 the arrangement originally proposed by way of a suggested “variation” involved getting in the former trust funds from the former trustees, and holding them upon wholly new trusts such as might be made by an absolute owner of the funds. Wilberforce J, as he then was, held that the court could not approve this. He said that the proposal went much too far “because it was not confined to dealing in a beneficial way with the special requirements of this infant [beneficiary] but seeks authorisation for a complete resettlement which could only be justified if the ‘benefit’ within the meaning of the Act”.

There are a number of CGT cases which deal with the difference between a resettlement and a mere variation. It is often difficult distinguish the two.

Blackburne J said in *Wyndham v Egremont* [2009] WTLR 1473 at para 22 — there is no “bright–line test” for determining whether a suggested arrangement amounts to a variation or a resettlement. The question is really whether it is possible to regard the settlement as basically the same.

### 3.2 Examples of applications under Variation of Trusts Act 1958

- **Wyndham v Egremont** [2009] EWHC 2076 (Ch)
  Court allowed a new perpetuity period where the old one was about to terminate. The termination would have deprived the life tenant’s son of an interest in the trust fund and triggered a substantial CGT charge. Such applications are becoming increasingly common.

- **Pemberton v Pemberton** [2016] EWHC 2345 (Ch)
  An elderly settlement (created in 1965) was given a thorough overhaul to make it fit for purpose in modern conditions. The court approved a new 125 year perpetuity period, added modern investment powers, and widened the class of beneficiaries to spouses including same sex and civil partners.

- **A v Band** [2016] EWHC 340 (Ch)
  The court approved a new perpetuity period of 125 years together with a power to accumulate income throughout that period. Changes of a more administrative nature were also included such as a power to take out trustee indemnity insurance and clarification of the self-dealing provisions.

- **Bernstein and Another v Jacobson** [2008] EWHC 3454 (Ch)
  The court consented to a variation of contingent legacies to allow the total funds to pass to the deceased’s widow on IPDI trusts thus obtaining the spouse exemption for the estate and increasing the

---

available ‘pot’. The IPDI in half of the increased pot would terminate after 2 years and the grandchildren would take absolute interests. The estate would insure against the possibility of the PETS to the grandchildren becoming chargeable if the widow died within 7 years. The case is interesting because the application was made during the administration of the estate before the trust had been constituted. The court was unconcerned that the motive of the variation was to achieve a tax saving.

- **Wright v Gater** [2011] EWHC 2881 (Ch)
  A postponement until the age of 30 of a 3 year old’s entitlement under the statutory trusts following the death of his father was inappropriate as it was close to being a resettlement. Nothing would remain of the original statutory trusts.

  A revised arrangement was approved that entitled the child to income at age 18, 10 per cent of the fund at 21 and the balance at 25. That arrangement was a variation rather than a resettlement,

- **Allfrey v Allfrey** [2015] EWHC 1717 (Ch)
  The court allowed an application to
  - allow trustees a power to accumulate income to meet inheritance tax anniversary charges, and
  - extend the perpetuity period.
  The changes would merely enhance the existing settlement, and were clearly a variation rather than a resettlement.

Note how many of the applications involve obtaining new perpetuity periods. Many existing settlements are nearing the end of their perpetuity period. Distribution of trust funds will often trigger heavy IHT and CGT charges so being able to prolong the life of the trust is very attractive. HMRC has so far not sought to be represented but it is perhaps surprising that there has been no attempt to argue that the new perpetuity period creates a new settlement with consequent tax charges.

### 4. Power to Add and Exclude Beneficiaries

This isn’t really an example of inadequate powers because most modern settlements deliberately identify a relatively narrow class of beneficiaries (eg children and remoter issue of the settlor) but then give the trustees a power to add further persons (including charities) to the class.\(^4\) They also give a power to exclude beneficiaries.

The power to add or exclude is normally given to the trustees, although sometimes it is reserved to the settlor during his lifetime (on death it passes to the trustees).

#### 4.1 Spouses and civil partners

\(^4\) It is important in the case of lifetime transfers to state that the Settlor and spouse cannot be added although it is permissible to have power to add a widow or widower.
Spouses and civil partners of children are generally not included in the class on the basis that they can be added if there is a reason to do so. ‘Spouse’ includes a same sex spouse but not a civil partner. Terms such as spouse, husband, wife, widow, widower do not include civil partners unless the instrument so provides. However, in the case of instruments created on or after 13 March 2014 when the Marriage (Same Sex Couples) Act 2013 came into force, such terms include same sex spouses unless the instrument states otherwise.

4.2 Issue

The term ‘issue’ normally includes straight line descendants and does not include step-children. See Reading v Reading [2015] EWHC 946 (Ch). However, in that case the particular circumstances required the court to construe the reference to ‘issue’ as including step-children but there was substantial evidence indicating that this was the testator’s intention.

4.3 Adopted children

In trust instruments post-dating Adoption Act 1949 adopted children are normally included, unless excluded. (Many standard precedents routinely exclude adopted and illegitimate children relying on the power to add them if desired although this is not necessarily what a settlor would want.)

Up till now, adopted children have not been included if the will or trust instrument predated the Adoption Act 1976 but Hand v George [2017] EWHC 533 (Ch) appears to have changed this.

Legislative history

The Adoption Act 1926 provided broadly that a child remained the child of his or her birth parents rather than becoming in law the child of their adoptive parents. Section 5(2) dealt with an adopted child’s entitlements to the estate of his natural and adoptive parents:

“5(2) An adoption order shall not deprive the adopted child of any right to or interest in property to which, but for the order, the child would have been entitled under any intestacy or disposition, whether occurring or made before or after the making of the adoption order, or confer on the adopted child any right to or interest in property as a child of the adopter, and the expressions "child," "children" and "issue" where used in any disposition whether made before or after the making of an adoption order, shall not, unless the contrary intention appears, include an adopted child or children or the issue of an adopted child."

The Adoption of Children Act 1949, s9 provided that adopted children were treated as the children of their adopters, as did the Adoption Act 1976, s39. However, the 1949 Act did not apply in relation to deaths or
dispositions made before the Act came into effect and Sch 2, para 6 to the 1976 Act contained a transitional provision that prevented the application of s39 to existing instruments, including wills.

In **Hand v George** [2017] EWHC 533 (Ch) adopted children claimed that their rights under the European Convention of Human Rights (ECHR) were breached by the failure of the 1949 and 1976 Acts to overturn s5(2) of the Adoption Act 1926.

For the claimants to succeed they had to show not only that they were victims of an infringement of the Convention but also that the Human Rights Act 1998 ('HRA') conferred on them a right to seek a remedy for that infringement in the domestic court.

The European Court of Human Rights has consistently held that Article 14\(^5\) in conjunction with Article 8\(^6\) precludes legislation which confers more limited rights on adopted children to their adoptive parents' estate, than are conferred on natural children.

Rose J agreed that the failure of the domestic authorities to ensure that s5(2) had no continuing effect in relation to wills construed after the ECHR came into force was a breach of the rights guaranteed by ECHR, art 14 in combination with art 8.

In **Hand v George** the testator died in June 1947 leaving his estate to his children for life with the remainder in each case to such of their child or children who attained the age of 21, if more than one then in equal shares. When the testator's son, Kenneth, died in 2008, he was the life tenant of half of the trust funds. He had two adopted children who would have inherited that half but for the fact that they were adopted. It was clear that their rights under the ECHR were infringed.

But was this retrospective interpretation appropriate? The issue of the retrospective application of the HRA was considered by the House of Lords in **Wilson v First County Trust Ltd (No 2)** [2003] UKHL 40. Lord Scott referred to the common law presumption that a statute is not intended to have retrospective effect but said that this was no more than a starting point. Section 3 of the HRA (So far as it is possible to do so, primary legislation and subordinate legislation must be read and given effect in a way which is compatible with the Convention rights) is retrospective in the sense that it expressly applies to legislation whenever enacted. Thus section 3 may have the effect of changing the interpretation and effect of legislation already in force. However, it would normally be inappropriate to allow it to have the effect of altering parties' existing rights and obligations.

---

\(^5\) No 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

\(^6\) Right to respect for private and family life.
Lord Rodger said at [201] “... an appropriate test might be formulated along these lines: Would the consequences of applying the statutory provision retroactively, or so as to affect vested rights or pending proceedings, be ‘so unfair’ that Parliament could not have intended it to be applied in these ways?”

Rose J held in *Hand v George* that it was not a retrospective application of the HRA to apply it in 2008 to determine whether on the proper construction of the will, Kenneth was to be treated as having died with two children or without any children. The only point in time at which that question had to be asked was when Kenneth died. The change in the claimants' rights brought about by them obtaining a right to equal treatment under the HRA in October 2000 was not so unfair as to prevent the interpretation of the statutes in a way that was consistent with the ECHR: (1) the children of the testator’s other son had always had inheritance rights which would be reduced if Kenneth had children and (2) as they had done nothing to avail themselves of the remainder interest they acquired under the testator’s will, their rights were not 'vested' in the sense used in *Wilson* to describe the kinds of rights that should not be interfered.

Paragraph 6 of Schedule 2 to the 1976 Act should, therefore, be read pursuant to HRA, s3(1) so that it complies with the claimants' Convention rights by construing it as if it read:

“Section 39

(a) does not apply to an existing instrument or enactment in so far as (i) it contains a disposition of property, and (ii) the beneficiary of the disposition has done something to avail himself or herself of the property right in question before the coming into force of the Human Rights Act 1998”.

Beneficiaries of a will or trust will normally have done nothing to avail themselves of inheritance rights so adopted children would appear to be generally able to inherit under instruments pre-dating the relevant legislation.
III. SECTION 144 OF THE INHERITANCE TAX ACT 1984

Section 144 provides that where property is settled by will and within two years of death, and before an interest in possession has arisen, an event occurs which would otherwise be chargeable to IHT, there will be no IHT and the deceased's estate will be treated for all IHT purposes as if the property had been left directly to the new beneficiary. In other words the trust disappears.

1. Uses of s144

1.1 Section 144 is useful as an aid to will drafting. It allows all or part of an estate to be left on discretionary trusts with a Letter of Wishes, achieving flexibility. It is commonly used for businesses where it is uncertain whether or not BPR will be available and many people are favouring the use of discretionary trusts as an alternative to detailed drafting to try to ensure the availability of the RNRB.

1.2 Since the introduction of the transferrable nil rate band, the section has been used to unscramble old fashioned wills for married couple which leave a nil rate band discretionary trust for the benefit of the family and residue to spouse.

Example
T leaves a sum equal to his available nil rate band on discretionary trusts for the benefit of his wife and family, residue to his wife. Eight months after his death the trustees appoint the nil rate sum to his wife. The discretionary trust will disappear and the whole estate will be treated as left to his wife and so will attract the spouse exemption.

1.3 The introduction of the RNRB means that s144 will also be used to appoint out of grandparental and other settlements to ensure that lineal descendants 'inherit' residential property.
Example
Grandma leaves her estate to such of her grandchildren as reach 21 (a relevant property trust). When she dies all of the grandchildren are minors. The trustees should use any express powers of appointment, or the statutory power of advancement, to appoint out a sufficient interest in a residence (probably on a revocable IPDI) to allow the estate to benefit from the RNRB.

2. **Section 144 cannot apply after an interest in possession has arisen**

The section states expressly that it cannot be used to modify the terms of a trust arising after the death of a surviving spouse with an IPDI.

Example
Fred leaves his estate which includes a residence to his second wife, Susan on IPDI trusts and then on discretionary trusts for his children and grandchildren from first marriage.

On Susan’s death the RNRB will not be available in relation to the residence held in the trust as lineal descendants of Susan are not beneficially entitled to the residence. Section 144 is no help on Susan’s death because there has been an interest in possession.

Instead the trustees should modify the terms of the trust during Susan’s lifetime to give one or more of the lineal descendants a beneficial entitlement.

3. **Who takes action under s144?**

Often the beneficiaries of a will trust attempt to join together and collectively vary the disposition of the property held in trust using IHTA 1984, s142. They can only do this if they are of full age and capacity and between them entitled to the whole beneficial interest, ie the rule in *Saunders v Vautier*.

---

7 The step-children and grandchildren are lineal descendants of Susan (IHTA 1984, s8K(3). The difficulty is that they are not ‘entitled’ as required by s8J(5).
Occasionally, this is the case; for example where the class of beneficiaries consists only of spouse and adult children. Much more frequently, though, the class includes minor and unborn beneficiaries. In such circumstances an application would have to be made to court under the Variation of Trusts Act to get the consent of the court on behalf of the minors and unborns. Without it a purported post-death variation is ineffective.

In such cases it is the trustees who should take action in which case s144 will apply.

Note that the executors and trustees are usually the same people but, if they are different, it is the trustees who act.

4. **Time limits**

4.1 **Reading back only within 2 years of death**

Events occurring more than 2 years after death are not read back.

For example, if trustees of a nil rate band discretionary trust appoint to a surviving spouse three years after the original death, thinking that they will secure a transferable nil rate band for the surviving spouse, this is not the case. The first spouse used his nil rate band. No nil rate band is transferred to the survivor but the property is now part of the survivor’s estate. Only a single nil rate band is available on the death of the survivor.

Consequence? The advisers are likely to be liable for the extra IHT.

**Note:** An appointment made more than 2 years from death can, however, often be beneficial from an income tax point of view. After that date, trustees can give beneficiaries revocable rights to income without creating an immediate post-death interest.

4.2 **Reading back in 3 months following death?**

When property leaves a discretionary trust within three months of creation, no IHT is payable. Therefore, as originally drafted, there was no reading back if the appointment was made within the first three months of death. This meant that an appointment to a spouse within that period did not attract the spouse exemption (the so-called *Frankland* trap).

The section was amended after FA 2006 to allow for reading back where property was appointed on life interest trusts or to bereaved minor trusts and s71D trusts. Different wording was used and here appointments can be made within three months of death and secure reading back.
It was amended again in Finance (No 2) Act 2015 to allow reading back where an appointment is made within the first three months for deaths on or after 10 December 2014.

5. Form of appointment

The section does not impose any requirements and indeed talks in terms of ‘events’ so an informal advancement of capital will suffice for s144.

However, the trust instrument will normally require the use of a deed to exercise a power of appointment. If a deed is not used the purported appointment will be invalid and ineffective.

The appointment will either identify the assets appointed expressly or if, as is often the case, the appointment is being made before the PRs have transferred specific assets to the trust, the trustees will simply appoint their rights to whatever they are entitled to under the deceased’s will.

Most settlements have an express clause allowing the advancement of trust property for the benefit of beneficiaries. But even where there are no such powers, Trustee Act 1925, s32 will apply giving a statutory power of advancement. As originally drafted the section allowed trustees to advance up to half of a beneficiary’s vested or contingent entitlement. This was widened by Inheritance and Trustees Powers Act 2014 for trusts created or arising on or after 1 October 2014 to allow trustees to advance the whole of a beneficiary’s entitlement to capital. Such a power does not require a deed or even writing.

Section 144 applies automatically. There is no need to claim reading back and no need to refer to s144 when exercising a power of appointment or advancement. An IHT 100 is not required. See IHT & Trusts Newsletter August 2008:

“Although the distribution may alter the amount of IHT on the death estate there is no need for the trustees to complete an IHT 100”.

6. CGT implications of appointment under s144

Section 144 deals only with IHT and there is no corresponding provision for CGT so normal CGT principles apply. An appointment from a trust resulting in a beneficiary becoming absolutely entitled as against the trustees is a deemed disposal which will give rise to a charge to CGT to the extent that the assets have increased in value since death.

It is, therefore, important for trustees and PRs to consider the CGT position. CGT manual deals with the position at CG31431 and CG31432.

Where the trustees exercise their powers of appointment AFTER the assets have vested in them then the assets concerned will already have passed out of the estate and into the hands of the trustees. In these circumstances the
exercise of the power of appointment to give a beneficiary an absolute entitlement as against the trustees will amount to a disposal for CGT purposes.

(In the case of a trust of residue assets will normally vest in the trustees when the administration of the estate is complete: that is when the residue is ascertained. The PRs may vest particular assets in the trustees before that date by assent or appropriation. In the case of non-residuary trusts, there will be an assent or appropriation.)

However, where the appointment is made BEFORE the PRs vest the assets in the trustees, HMRC accepts that the appointment is to a person who takes as legatee rather than as a beneficiary of a trust. This means that CGT is not payable. See Capital Gains Tax Manual, para 31432:

“Where the trustees exercise their powers of appointment before the assets have vested in them then the assets are still in the hands of the personal representatives at the time of the exercise. Even though these may be the same individuals as the trustees they are different bodies of persons for CGT purposes, see CG31110–CG31123. If, in these circumstances, the trustees make an appointment under the specific powers given to them in the will, then when the asset(s) vest they should be treated as passing direct to the appointee.

The asset(s) appointed should be treated as never becoming subject to the trust. In effect, the appointment is read back into the will. It is treated as though the deceased had intended the assets concerned to pass directly to the legatee rather than into trust. The appointee then takes those asset(s) as legatee and therefore acquires the asset(s) at probate value by reason of Section 62(4) TCGA 1992, see CG31140+.

Where assets have increased substantially since the date of death, trustees should make the appointment before the assets have vested to avoid an unnecessary tax liability.

Wills commonly provide that trustees can exercise their powers of appointment before completion of the administration of the estate but it does not seem that this is necessary. In such a case, the trustees would word the appointment as an appointment of their right to the property left to the trust in the will. However HMRC like to see this power so it is best to include it when drafting wills.
APPENDIX 1

APPOINTMENT CREATING RIGHT TO INCOME

THIS DEED OF APPOINTMENT is made the [ ] day of [ ] 20[ ] by [ ]
('the Appointors').

SUPPLEMENTAL to a deed of settlement dated [ ] and made between [ ]
('the Settlement')

RECITALS

A. By clause [ ] of the Settlement the Trustees have power to appoint
capital and income of the Trust Fund amongst such of the
Beneficiaries as they may see fit. The power is exercisable and any
exercise may be made revocable during the Trust Period.

B. B is a member of the class of Beneficiaries.

C. The Appointors are the present Trustees of the Settlement and the
Trust Period has not expired.

NOW THIS DEED WITNESSES

1. Definitions
   In this Deed ‘the Trustees’, ‘the Trust Period’, ‘the Trust Fund’ and
   ‘the Beneficiaries’ shall have the meaning given to these terms in the
   Settlement.

2. Exercise of power of appointment
   In exercise of the power of appointment conferred on them by clause
   [ ] of the Settlement and of all other relevant powers the Appointors
   hereby appoint that from and after the date hereof the Trust Fund
   shall be held on trust to pay the income thereof to B for his life.

3. Power of revocation reserved
   The Trustees may at any time or times during the Trust Period by
deed or deeds revoke or vary either wholly or in part the appointment
contained in clause 2 above.

4. Exclusion of apportionment of income
   All income of the Trust Fund received by or on behalf of the Trustees
from and after the date of this Deed shall be treated as if it had
arisen wholly after such date and no apportionment of income shall
be required.

IN WITNESS etc.

---

8 The Trusts (Capital and Income) Act 2013 makes this clause unnecessary for trusts created on or after 1
October 2013 as it disapplies the apportionment rules. However, it is sensible to include a general statement
that apportionments are not required in the interests of clarity.
REVOCATION AND NEW APPOINTMENT TO CHANGE THE INTEREST IN
POSSESSION BENEFICIARY

THIS DEED OF REVOCATION AND APPOINTMENT is made the [ ] day of [ ]
20[ ] by [ ] (‘the Appointors’).

SUPPLEMENTAL to:

1. a deed of settlement dated [ ] and made between [ ] (‘the Settlement’)
2. a revocable deed of appointment dated [ ] and made by the Appointors
   (‘the Revocable Deed’).

RECITALS

A. By clause [ ] of the Settlement the Trustees have power to appoint capital
   and income of the Trust Fund amongst such of the Beneficiaries as they
   may see fit. The power is exercisable and any exercise may be made
   revocable during the Trust Period.

B. By Revocable Deed [B] a member of the class of Beneficiaries was
   appointed a life interest in the income of the Trust Fund.

C. The Appointors are the present Trustees of the Settlement and are desirous
   of revoking the Revocable Deed and making such new appointment as is
   set out below.

D. The Trust Period has not expired.

NOW THIS DEED WITNESSES

1. Definitions

   In this Deed ‘the Trustees’, ‘the Trust Period’, ‘the Trust Fund’ and ‘the
   Beneficiaries’ shall have the meaning given to these terms in the
   Settlement.

2. Revocation of Revocable Deed

   In exercise of the power reserved to them the Appointors hereby revoke in
   its entirety the Revocable Deed.

3. Exercise of power of appointment

   In exercise of the power of appointment conferred on them by clause [ ] of
   the Settlement and of all other relevant powers the Appointors hereby
   appoint that from and after the date hereof the Trust Fund shall be held on
   trust to pay the income thereof to C for his life.

4. Power of revocation reserved

   The Trustees may at any time or times during the Trust Period by deed or
   deeds revoke or vary either wholly or in part the appointment contained in
   clause 3 above.
5. **No apportionment of income**

   All income of the Trust Fund received by or on behalf of the Trustees from and after the date of this Deed shall be treated as if it had arisen wholly after such date.

IN WITNESS etc.

---

9 The Trusts (Capital and Income) Act 2013 makes this clause unnecessary for trusts created on or after 1 October 2013 as it disapplies the apportionment rules. However, it is sensible to include a general statement that apportionments are not required in the interests of clarity.