Analysis
Futter & Pitt: the *Hastings-Bass* principle

SPEED READ **The Supreme Court has comprehensively reviewed the *Hastings-Bass* principle in *Futter v HMRC, Pitt v HMRC*. The principle remains an important remedy, but it is discretionary and will not apply where the applicants have properly relied on professional advice which has turned out to be incorrect. In the future, the court is likely to refuse to use its discretion to provide relief in cases involving tax avoidance.**

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The Supreme Court's judgment in the joined cases of *Futter and another v HMRC, Pitt and another v HMRC* [2013] UKSC 26 was given on 9 May 2013, providing an authoritative view of the *Hastings-Bass* principle (the 'principle'). The decision was unanimous, largely confirming the Court of Appeal's previous decision. Lord Walker gave the leading judgment. The cases involved applications by trustees (Futter) and by a Mental Health Act receiver (Pitt) for certain transactions to be set aside under the principle and, in the case of Pitt, on the alternative ground of mistake. This article considers the decisions only in relation to the principle.

The Court of Appeal decision

Before the decision in *Futter & Pitt,* CA, the principle was thought to be founded on Lord Justice Buckley's summary in *Re Hastings-Bass (deceased)* [1974] STC 211. Lord Justice Buckley's negative formulation was subsequently expressed in positive terms in *Mettoy Pension Trustees Ltd v Evans and others* [1991] 2 All ER 513, and in the case of *Sieff v Fox* [2005] EWHC 1312, Lord Justice Lloyd, who later gave the leading judgment in *Futter & Pitt*, CA, summarised the principle (at para 49) as follows: 'Where a trustee acts under a discretion given to him by the terms of the trust, but the effect of the exercise is different from that which he intended, the court will interfere with his action if it is clear that he would not have acted as he did had he not failed to take into account considerations which he ought to have taken into account, or taken into account considerations which he ought not to have taken into account.'

The Supreme Court judgment

The Supreme Court found that the *Hastings-Bass* principle was not actually founded upon the decision in *Re Hastings-Bass,* because Lord Justice Buckley's summary of the principle in that case was not actually the ratio decidendi of his decision.

That was important because Lord Justice Buckley's formulation included within the one principle acts which are 'unauthorised by the power conferred on' the trustee and acts based on inadequate or improper consideration. In *Futter & Pitt*, SC, Lord Walker characterised these two categories as 'excessive execution' and 'inadequate consideration'. It is clear from authority that acts of excessive execution are void (see paras 9, 25 and 233). If both acts of excessive execution and acts of inadequate consideration fell within the principle, it would be difficult to see why the latter should only be voidable if the former are void. As we shall see, the Supreme Court was determined that acts falling within the principle should be voidable rather than void.

The decision of the Supreme Court, and the prior decision of the Court of Appeal, therefore, depended upon making a clear distinction between the categories of excessive execution and inadequate consideration.

Breach of duty

The formulations of the principle in *Re Hastings-Bass, Mettoy* and *Sieff* all require there to be either a failure to take account of something, or the taking account of something of which account should not have been taken. It was uncertain whether this required the failure to amount to a breach of duty. In *Futter & Pitt*, the Supreme Court agreed with the Court of Appeal that breach of duty was an essential condition of the principle applying.

In what circumstance would an action to which trustees give inadequate consideration and which results in a sufficient loss to a trust fund to justify an application to the court, not involve a breach of trust by the trustees? Lord Walker considered two possibilities. First, he considered the situation where the trustees rely on expert advice. In both *Futter* and *Pitt*, he found that there was no breach because the trustees (in *Futter*) and the fiduciary (in *Pitt*) had properly relied on expert advice which happened to be incorrect. He therefore found that the principle could not apply in either case. In *Pitt*, however, he found for the appellants and against HMRC on the alternative ground of mistake.

Secondly, he considered the situation where a trust includes an exoneration clause, under which the trustees are excused from liability for a breach made in good faith. Lord Walker records the argument of counsel for HMRC that an exoneration clause does not prevent a trustee being in breach. Although the trustee may be relieved of liability for that breach, other consequences of the trustee being in breach will not be excluded; for example, injunctive relief to prevent a threatened breach of trust, and personal and proprietary remedies against persons who receive assets wrongly distributed (paras 19 and 89).

Lord Walker did not expressly conclude that there can never be a situation in which an exoneration clause might have the effect that the trustee is not in breach of his duty as a trustee with the result that the principle could not apply.

However, he did say (at para 89) that: 'The Futter No. 3 and No. 5 settlements contain exoneration clauses in conventional terms ... I would not treat ... [those clauses] ... as ousting the application of the *Hastings-Bass* rule, if it were otherwise applicable.'

Void or voidable

The formulation of the principle in *Mettoy* and *Sieff* is that, where the conditions of the principle are satisfied, 'the court will interfere with [the trustees'] action'. That does not specify the action which the court will take but it does not seem to allow the court to take no action at all. If the court finds that an act is void, it finds that it has, in law, never taken place. If an act is voidable, it will be fully effective, unless a beneficiary applies to the court for the act to be voided. In that case, whether and to what extent a remedy should be applied is at the discretion of the court and is subject to the normal equitable bars, laches, complicity and acquiescence.

The Supreme Court found that when the principle applies, the impugned transactions are voidable (para 43).

The effect of a voidable transaction being voided

When the court exercises its discretion to void a transaction, it seeks to put the parties into the position they would have been in had the voided transaction not taken place, subject to preserving the rights of bona fide third party purchasers for value. The tax authorities are not in the position of a bona fide third party purchaser for value without notice. Taxation is a statutory consequence of a transaction taking place.

In the Court of Appeal in *Futter & Pitt*, Lord Justice Lloyd said (at para 91): 'As a general proposition (which is probably an over-simplification), tax is due on or as a result of transactions which are effective, not those which are not. In the case of IHT, a specific provision [IHTA 1984 s 150] … means that it does not matter whether a transaction is void or is set aside as voidable. In either case, any tax paid on the transaction is to be repaid and any calculation made by reference to the transaction is to be redone without reference to it. [Counsel for HMRC] told us that, without making any concession, he understood the position to be likewise in respect of other taxes. That may not be so in every case, but in principle it seems to be right, even though principle may not always be the decisive factor in relation to fiscal legislation.'

It would seem, therefore, that for fiscal purposes, the effect of a transaction being voided under the principle is likely to be that it is treated as if it had not occurred, although that simple rule may be subject to variation, in a manner which will be explored in later cases, where it is not possible for the court to achieve a restitutio in integrum (paras 8 and 58).

Is tax a special case?

Lord Walker in the Supreme Court referred with approval (at paras 58 and 63) to the Court of Appeal's consideration of the duties of trustees in exercising their discretion, and in particular the relevance of tax considerations. It is clear that tax is a consideration which, in appropriate circumstances, trustees may have a duty to take into account.

How will the court exercise its discretion in tax avoidance cases?

Because the Supreme Court has held that transactions within the principle are voidable and not void, where the conditions of the application of the principle are satisfied, the court will have discretion as to whether or not to grant a remedy.

In the part of his judgment specifically dealing with *Futter,* Lord Walker considered how the Court might exercise its discretion in respect of the doctrine of mistake, in relation to transactions which were intended to be tax avoidance transactions. Lord Walker said: 'there would have been an issue of some importance as to whether the court should assist in extricating claimants from a tax-avoidance scheme which had gone wrong. The scheme adopted by Mr Futter was by no means at the extreme of artificiality ... but it was hardly an exercise in good citizenship. In some cases of artificial tax avoidance, the court might think it right to refuse relief, either on the ground that such claimants, acting on supposedly expert advice, must be taken to have accepted the risk that the scheme would prove ineffective, or on the ground that discretionary relief should be refused on grounds of public policy. Since the seminal decision of the House of Lords in *WT Ramsay Ltd v IRC* [1982] ... there has been an increasingly strong and general recognition that artificial tax avoidance is a social evil which puts an unfair burden on the shoulders of those who do not adopt such measures. But it is unnecessary to consider that further on these appeals.'

The view that tax avoidance is 'a social evil' is startling and seems to have less to do with the movement of opinion in the 32 years since *Ramsay* than with the volatile state of public opinion since the financial crash of 2008. It contrasts oddly with the decision in *Hastings-Bass*, where the court found for the trustees in refusing to regard their entire transactions as a nullity, in circumstances where to do so would have resulted in a large liability to estate duty. In that case, the impugned transactions were part of: 'a scheme which was described by Captain Hastings-Bass in a contemporary letter as "a scheme whereby some of the enormous death duties may be reduced on the settlement"' (*Re Hastings-Bass (deceased) v IRC* [1974] STC 211 at p 215).

As the Supreme Court has held that, where the principle applies, the impugned transactions are voidable not void, similar issues will arise in the court's determination of the appropriate remedy as arise in mistake. Applications seeking to avoid transactions undertaken for tax avoidance purposes which have turned out to have deleterious taxation results are unlikely, any longer, to benefit from the court's exercise of its discretion. ■

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Cases: *Futter & Cutbill v HMRC* (Alan Dolton, 15.5.13)

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