

declared that certain dispositions of property made by a deceased within 3 years of his death fell outside the charge to estate duty.

Background

In December 1989 Mr Pong Ten Un ("Mr Pong") was 85 years old and suffering from cancer. He had been ill for some years. In that month 5 unit trusts were set up in the Isle of Man. The sole trustee of those unit trusts was a Manx company incorporated in the same month called Shiu Wing Ltd ("SWL"). The directors of SWL were Mr Pong's wife ("Mrs Pong") and his 7 children Harry, Frank, David, Edward, Stanley, Elizabeth and Teresa. The sole shareholders of SWL were two other Manx companies : *Shiu Kwong Ltd* (whose directors were Harry, Frank, David and Edward) and *Futurian Ltd* (whose directors were Mrs Pong, Stanley, Elizabeth and Teresa). At about the same time discretionary trusts were set up in the Isle of Man for the benefit of the children; the trustees of those discretionary trusts were Shiu Kwong Ltd and Futurian Ltd (hereafter to be referred to as "the discretionary trustees").

At that time (December 1989) Mr Pong owned properties in Hong Kong which, upon his death, would have passed to his Hong Kong estate and would have attracted estate duty under s.5 of the Estate Duty Ordinance, Cap. 111. By s.6(1)(c) property passing on the death of a deceased is deemed to include property :

"... taken under a disposition made by him, purporting to operate as an immediate gift inter vivos, whether by way of transfer, delivery, declaration of trust, or otherwise, which shall not have been bona fide made 3 years before the death"

The properties owned by Mr Pong fell into two categories :

1. 1. shares in various Hong Kong private companies, in particular shares in Shiu Wing Steel Ltd (held directly and through a holding company) which operated the largest steel mill in Hong Kong; and
2. 2. real estate : (a) a property called the Hillview property and (b) Yau Tong Inland Lot No. 4 ("the YTIL property") where the steel mill was located.

At that time there were various factors at play which caused Mr Pong to enter into the transactions which gave rise to the present litigation. These are summarized in Godfrey JA's judgment as follows :

"There was uncertainty as to the future of the commercial operations in Hong Kong of Shiu Wing Steel Limited; including a possibility of the transfer of some or all of its operations to Canada; there was uncertainty as to the political and economic risks (including possible exchange control measures) attendant on the resumption in 1997 by the People's Republic of China of sovereignty over Hong Kong; and there were others. These considerations indicated a need for the deceased (and his children) to take measures for the protection of their assets. And, in 1990, the deceased was some 85 years old and suffering from cancer. This indicated a need for the deceased to take estate planning measures to avoid or mitigate the incidence of estate duty on his death. The deceased's motives, or reasons, for acting as he did cannot fairly be characterised as purely or solely fiscal. His motives were mixed; his reasons for acting as he did were partly fiscal and partly non-fiscal."

The transactions

Two sets of transactions are involved in the present litigation : (1) Transactions effected on 25 January 1990 and (2) transactions relating to the YTIL property on 24 October 1990.

In essence, the transactions which Mr Pong entered into on 25 January 1990 were as follows :

The shares

1. These were sold to SWL as trustee for the various unit trusts for a total of \$65,542,894.
2. Mr Pong then lent the proceeds of sale to the discretionary trustees.
3. With these loans the discretionary trustees applied for units in the unit trusts held by SWL. Units were accordingly allotted.

The Hillview property

1. Mr Pong sold the Hillview property to SWL as trustee for the Hillview Unit Trust for \$42.2m.
2. The proceeds of sale, received in Macau, were given in Macau as a gift to Shiu Kwong Ltd and Futurian Ltd as trustees of the Pong Ding Yuen Trust.
3. Using this sum of \$42.2m the trustees of the Pong Ding Yuen Trust applied to SWL for units in the Hillview Unit Trust. Units were accordingly allotted.

Pausing here, if nothing else were said, the effect of these transactions seen from the estate duty point of view would have been as follows : As regards the shares, Mr Pong would have divested himself of his ownership in the Hong Kong shares upon sale to SWL and he would have acquired specialty debts owed by the discretionary trustees in the Isle of Man; those two companies (Shiu Kwong Ltd and Futurian Ltd) would have owned units in the various unit trusts held by SWL, a Manx company; in effect, the ownership of the shares would have transferred from Mr Pong to SWL in consideration of the off-shore debts. The units allotted to the discretionary trustees (in consideration of the payment of money lent to the discretionary trustees by Mr Pong) would likewise be offshore assets. These would not be property which attracted estate duty upon Mr Pong's death, as s.10(b) provides that estate duty shall not be payable in respect of property situate outside Hong Kong. It is common ground that *factually* that is what did happen as regards Mr Pong's shares on 25 January 1990. So the appellants ask quite simply this : Why should the Court not give effect to the legal consequences of these admittedly genuine transactions in applying the provisions of the Estate Duty Ordinance?

As regards the Hillview property, Mr Pong would have transferred ownership of the property to SWL upon sale and would have then given the proceeds of sale to the Pong Ding Yuen Trust in Macau which, with that sum, would have acquired units in the Hillview Unit Trust. The gift which Mr Pong made was of property situated in Macau, not Hong Kong : Hence, even if he were to die within 3 years, the gift would have fallen outside the scope of s.6(1)(c). Again the appellants ask : Why should legal effect not be given to these transactions in applying the Estate Duty Ordinance?

As regards the YTIL property, Mr Pong entered into the following transactions on 24 October 1990 :

1. The YTIL property was sold to SWL as trustee for the YTIL Unit Trust for \$139m.
2. Mr Pong lent the proceeds of sale to the discretionary trustees.
3. With the loans the discretionary trustees applied for units in the YTIL Unit Trust. Units were accordingly allotted.

Again, pausing here, if nothing else were said, the effect of these transactions seen from the estate duty point of view would have been simply this : Mr Pong would have divested himself of his ownership in the YTIL property upon sale to SWL and would have acquired specialty debts located in the Isle of Man : No estate duty would have been payable in respect of these specialty debts upon his death : see s.10(b).

The Estate Duty Commissioner's case

The Estate Duty Commissioner does not challenge the genuineness of the transactions, as summarized above, and accepts that they did in fact take place. He says however that when other factors are put into the equation and the principles of construction developed in *W T Ramsay Ltd v. IRC* [1982] AC 300 are applied, it can be seen that in reality what Mr Pong did on 25 January and 24 October 1990 was to have made immediate gifts of his Hong Kong shares and properties to his children by way of settlements upon trust : Since he died, unfortunately, on 23 January 1993, three days short of the 3 years provided for in s.6(1)(c), all the shares and properties became assessable to estate duty.

The factors omitted from the above summaries are these. SWL had no money. The money movements, which resulted in SWL acquiring the Hong Kong shares and properties, and issuing units to the discretionary trustees, were circular. On 25 January Mrs Pong borrowed \$139m from the Standard Chartered Bank in Macau. This was unsecured. No interest was paid. The money was lent to SWL which then initiated the transactions as summarized above. The money then came back to SWL as the consideration for the allotment of units to the discretionary trustees; thus Mrs Pong was repaid and she in turn repaid the bank. What the bank statements reveal is that for each transaction one complete cycle of money movements was used : from Mrs Pong, and then back to Mrs Pong; and when all the transactions were completed Mrs Pong paid back the money to the bank. As everything was pre-ordained the completion of these cycles would have taken very little time. It all happened on the same day. Although Mrs Pong borrowed \$139m on 25 January, in fact the total consideration for the various transactions on that day (the transfer of the shares and the Hillview property) came to only \$107,745,894 : This, the Commissioner argues, demonstrates how artificial it all was. Essentially, an operation identical to those relating to the shares was repeated vis-a-viz the YTIL property on 24 October.

Moreover, the Commissioner points out, on 25 January 1990 Mr Pong made a will in which he forgave the specialty debts owed by the discretionary trustees at his death; then in October 1991 he formally released the first lot of specialty debts (created in January 1990) and in October 1992 he released the further specialty debts created on the transfer of the YTIL property.

The units in the various unit trusts held by SWL were allotted, as mentioned earlier, to Shiu Wing Ltd and Futurian Ltd as trustees of discretionary trusts for the children. The Commissioner therefore contends thus : There were, on 25 January and 24 October, composite transactions which were pre-ordained; estate-duty-driven steps were inserted which, if disregarded, would show that, on 25 January and 24 October, Mr Pong had simply

made immediate gifts of his Hong Kong shares and properties to his seven children : The fact that they were *conditional* gifts - conditional upon SWL issuing units of corresponding value to the trustees of the discretionary trusts for the benefit of the children - makes no difference : Another way of putting the same proposition is that Mr Pong had, according to the Commissioner, made gifts of his shares and properties with a direction to SWL to issue the requisite units to the trustees of the discretionary trusts. This being the "underlying reality" of the transactions, a purposive construction of the Estate Duty Ordinance, according to the principles enunciated by the House of Lords in *Ramsay*, leads to the conclusion that the various transfers of properties must be treated as transfers by way of gift *inter vivos*, within the meaning of that expression in s.6(1)(c).

The Ramsay principle

It is necessary at the outset to emphasize, as Lord Steyn said in *IRC v. McGuckian* [1997] STC 908 at 916e, that the *Ramsay* principle is not invented on a juristic basis independent of statute : "That would have been indefensible since a court has no power to amend a tax statute. The principle was developed as a matter of statutory construction".

In *Ramsay* itself the taxpayer had, upon the sale of farm land, realised a chargeable gain. For the sole purpose of avoiding the capital gains tax which would have been payable the taxpayer entered into a ready-made scheme (bought from a company specializing in such schemes) to create an artificial capital loss. The scheme itself was self-cancelling, and looked at as a whole, there was neither gain nor loss. The House of Lords concluded that, in these circumstances, the scheme, for the purposes of the relevant taxing statute, had to be disregarded. As Lord Wilberforce said at 326E :

"The capital gains tax was created to operate in a real world, not that of make-belief ... it is a tax on gains ... it is not a tax on arithmetical differences. To say that a loss (or gain) which appears to arise at one stage in an indivisible process, and which is intended to be and is cancelled out by a later stage, so that at the end of what was bought as, and planned as, a single continuous operation, there is not such a loss (or gain) *as the legislation is dealing with*, is in my opinion well and indeed essentially within the judicial function" (emphasis added).

As can be seen from the passage above, Lord Wilberforce reached his conclusion (that the scheme was artificial and had to be disregarded) as a matter of construction of the relevant taxing statute.

Furniss v. Dawson

In *Ramsay*, what was disregarded as a fiscal nullity was a circular self-cancelling scheme. The principle was applied in what has been described as a "linear" transaction in *Furniss v. Dawson* [1984] 1 AC 474. There Mr Dawson and members of his family owned the shares in two operating companies which manufactured clothing. They had agreed in principle to sell their shareholdings to a purchaser. Upon the completion of the sale they would have been liable to pay capital gains tax. In order to defer such tax liability they entered into a scheme whereby they exchanged their shareholdings for shares in a Manx company which in turn then sold the shareholdings to the purchaser. The series of transactions was pre-ordained.

Section 19 of the Finance Act 1965 charged tax in respect of capital gains accruing to a person on the *disposal* of assets. Schedule 7 para. 6(2) provided certain exceptions in the case of company amalgamations. One exception applied to shares transferred to another company

which thereby acquired control, in exchange for shares in the transferee company. In such a case there was deemed to be no *disposal* of the former shareholding : The new shareholding and the old shareholding were to be treated as the same asset : see Lord Brightman's speech at 520E. The taxpayers therefore argued thus : As they had transferred their shareholdings to the Manx company in exchange for shares and as that company had acquired control of the operating companies, there was no "disposal" of assets which attracted capital gains tax; charge to capital gains tax should be deferred until such time as they disposed of their shares in the Manx company and thereby realized a capital gain. The control of the operating companies by the Manx company was, of course, only a fleeting phenomenon, since the Manx company, in accordance with the pre-ordained scheme, simultaneously sold the shareholdings to the purchaser. The *reality* of the transactions, as can be seen, was that the taxpayers, through their 100% control of the Manx company, received the purchase price for the sale of their shares in the operating companies : It was, as Lord Fraser of Tullybelton puts it at 513E, a disposal by the taxpayers of the shares in the operating companies for cash to the purchaser.

The House of Lords concluded that, in these circumstances, the insertion of the Manx company had to be disregarded and the end result must be looked at and taxed according to the statute in question. To apply the *Ramsay* principle, in these circumstances, there must be the following (as per Lord Brightman at 527D-E) :

"First, there must be a pre-ordained series of transactions; or, if one likes, one single composite transaction. This composite transaction may or may not include the achievement of a legitimate commercial (i.e. business) end. The composite transaction does, in the instant case; it achieved a sale of the shares in the operating companies by the Dawsons to Wood Bastow [the purchaser]. It did not in *Ramsay*. Secondly, there must be steps inserted which have no commercial (business) purpose apart from the avoidance of a liability to tax - not "no business *effect*." If those two ingredients exist, the inserted steps are to be disregarded for fiscal purposes. The court must then look at the end result. Precisely how the end result will be taxed will depend on the terms of the taxing statute sought to be applied."

As a general statement of principle in construing a taxing statute, there can be no quarrel with Lord Brightman's formulation. The *Ramsay* principle enjoins the court to look to substance rather than to form. As Lord Bridge of Harwich remarked at 517F, it would need no more than a cursory exposition of the avoidance scheme in *Ramsay* to lead any intelligent layman to conclude that the scheme was not designed to achieve any substantial effect in the real world and that the elaborate steps designed to manufacture a tax deductible loss was purely formal in character. And, in *Furniss v. Dawson* itself, the Manx company's control of the operating companies was for a split second only, in order to found that company's claim to have been in control of the operating companies for the purposes of para. 6(2) of Schedule 7 to the Finance Act 1965. Such a step was purely formal and had no effect on the substance of the composite transaction : see Lord Bridge at 518E.

After Furniss v. Dawson

Since *Furniss v. Dawson* there have been a number of cases in England elaborating upon the *Ramsay* principle, and the English courts have been grappling with the consequences of extending that principle. Lord Oliver of Aylmerton, commenting upon *Furniss v. Dawson* in *Craven v. White* [1989] AC 398 at 501E-F, said :

"Now it has, I think, to be accepted that *Furniss v. Dawson*, whilst it purported to do no more

than apply the *Ramsay* principle to a different set of facts, involved in fact an extension of the principle and it did so not simply because it applied the principle to a "linear" transaction as opposed to a circular transaction. The *Ramsay* principle is simply that you look at the result which the parties actually intended to and did produce and apply to it the ordinary fiscal consequences which flow from that result. *Furniss* involved going a considerable step further than this and, by reconstituting the actual constituent transactions into something that they were not in fact, attributing to the parties an intended result which they did not in fact intend. To that unintended result there are then attached the fiscal consequences which would have flowed if the transaction had actually taken the form into which it is deemed to be reconstituted. It has to be borne in mind that the particular transaction with which *Furniss* was concerned, and with which each of the three appeals before your Lordships is concerned, was one in which an actual exchange of shares had taken place, a transaction which had permanent legal and fiscal results and to which certain fiscal provisions applied from the moment at which the transaction was effected. The critical question is that of identifying the circumstances in which such a transaction can be simply ignored and in which so radical a reconstruction of the actual events as that undertaken in *Furniss v. Dawson* is permissible and is to be undertaken by the court and whether, apart from the concept of tripartite contract upon which reliance was placed in reaching the decision in *Furniss*, such a reconstitution is rationally and logically possible within the accepted principles of construction provided by *Ramsay* or, indeed, any other principle."

What is clear from this and other similar passages in *Craven v. White*, and in later cases such as *Fitzwilliam v. IRC* [1993] STC 502 and *IRC v. McGuckian* [1997] STC 908, is that the court seeks to apply the relevant taxing statute to "the actual transaction the parties were effecting in the real world" (per Lord Browne-Wilkinson in *Fitzwilliam* at 535C) rather than the artificial devices in which the parties chose to clothe it "in the surreal world of tax advisers". Ultimately, what the court has to look at is the end result; how the end result will be taxed will depend upon the terms of the relevant taxing statute.

Application of the Ramsay principle

As mentioned earlier, the *Ramsay* principle concerns the approach to the proper construction of a taxing statute. Here, one starts with s.10(b) which exempts from estate duty property situate outside Hong Kong. If a deceased manages to arrange his affairs so that, at his death, he (or she) has no property situate within Hong Kong then - s.6(1)(c) apart - his estate is not chargeable to estate duty. There is no principle of law which requires the court to unravel his affairs upon his death in order to notionally bring property, otherwise outside the scope of estate duty, within the net.

Viewing, first of all, the transactions concerning the transfer of the shares to SWL as trustee for the various unit trusts, there can be no doubt what the *intended* result was: The shares were to be vested in SWL, and the discretionary trustees were to be allotted units in those unit trusts. There were good reasons for these steps apart from avoiding estate duty, as set out in Godfrey JA's judgment quoted earlier. There arose, as between Mr Pong on the one hand and the discretionary trustees on the other hand specialty debts created in the Isle of Man. These were not shams. The parties intended to give effect to the transactions in precisely the way they were structured. The identical remarks apply to the YTIL property.

As regards the Hillview property, the *intended* result was that the property was to be vested in SWL as trustee for the Hillview Unit Trust, and units were to be allotted to the discretionary trustees. The proceeds of sale were given in Macau to the discretionary trustees.

Assuming that the circular movements of money were disregarded as being artificial or

fictional, what then is the end result? As reconstructed, it would simply be that Mr Pong transferred his Hong Kong shares and properties to SWL with a direction to SWL as trustee to issue units in the various unit trusts to the discretionary trustees. That would not be a gift of Hong Kong property but of foreign property.

In my judgment, it is no answer to the point to say that the beneficiaries, being all *sui juris*, could have put an end to the trusts and claimed the underlying assets under the rule in *Saunders v. Vautier* [1841] 4 Beav. 115, 10 LJ.Ch. 354. As Rogers JA in the Court of Appeal aptly remarked, the purpose of establishing the trusts was presumably because the members of the Pong family did not wish to own assets in their personal names and wanted the trust structure.

Moreover, as Lord Keith said in *Fitzwilliam v. IRC* at 515a :

"No case applying the *Ramsay* principle has yet held it to be legitimate to alter the character of a particular transaction in a series or to pick bits out of it and reject other bits. In *Furniss v. Dawson* the transfer to the intermediary company ... was disregarded for fiscal purposes because of the pre-existing informal agreement and of the manner in which the two transactions were carried out, which made it intellectually possible to hold that [the intermediary company] *never had control of the operating companies within the meaning of the statute*. No comparable exercise is possible here." [emphasis added]

When Godfrey JA said in the Court of Appeal that "the real transaction here, the 'end result', was a gift of Hong Kong property by the deceased to his children" he was plainly wrong. Upon no process of "reconstruction", applying the *Ramsay* principle, could such a conclusion be reached.

Mortimer VP said this :

"The end result of the series of 21 transactions and the paper movement of money at the bank, followed by the release of the debts or transfer of the proceeds abroad (anticipated in the deceased's Manx will) was that the deceased *transferred his Hong Kong property to trustees of his family abroad*. The question arises whether there was any commercial or non-fiscal purpose for any of the elaborate steps taken in the course of achieving this straightforward result."

This calls for two observations :

1. If the release of the debts took place as intended - as Mortimer VP suggests - then it logically follows that there were *real* debts in the first place.
2. The statement "the deceased transferred his Hong Kong property to trustees of his family abroad" is incomplete : If the transfers were upon *sale*, then in regard to "an immediate *gift* inter vivos" under s.6(1)(c) the question must arise : Gift of what? Of the units in the unit trusts? Of the proceeds of sale? Mortimer VP is silent on these questions, which lie at the heart of the issue.

Circular movement of money

Earlier, I had proceeded on the assumption that the *Ramsay* principles applied, and that the circular movement of money might be disregarded : Nevertheless, the end result does not bring the case within the charge to estate duty.

I would, on the facts of this case, go further. Whilst it is possible - and perhaps right - to categorise the movement of money within the family and the family trusts as "artificial", the involvement of the bank cannot be so categorised. Between Mrs. Pong and the bank, a relationship of debtor and creditor was undoubtedly created. The sums credited to Mrs Pong's bank account, as shown in the bank statements, must necessarily be reflected in the bank's own books. Those transactions were real. They cannot be categorised as illusory. Accordingly, when SWL purchased Mr Pong's shares and properties, SWL was using "real" money - advanced to it by Mrs Pong. There is no reason to categorise that transaction as fictitious when "real" money was available, and was in fact lent. *Furniss v. Dawson* is not an authority for the proposition that whenever the court finds transactions of this kind, they must be disregarded. The question in *Furniss v. Dawson* was whether the Manx company ever acquired *control* of the operating companies *within the meaning of the Act* (see Lord Brightman at 520H). There is no comparable question in this case. If the question is : Did Mrs Pong in fact lend money to SWL, the answer surely is : Why not, since she had the money available from the bank? It is far too facile an approach to say "It is all smoke and mirrors" : a term used in Godfrey JA's judgment. As Findlay J at first instance remarked : "A tax should not be imposed by the courts; it should be made clear what it is specifically that the taxpayer did that renders him liable to the tax."

In my judgment there are no grounds for saying that the *Ramsay* principles applied in the circumstances of this case.

s.6(1)(c) Estate Duty Ordinance

The legal position quite simply is this. The properties which the deceased disposed of within 3 years of his death, by way of *immediate gift inter vivos*, were (a) the specialty debts released in October 1991 and October 1992 and (b) the gift of \$42.2m in Macau on 25 January 1990. They fall outside the charge to estate duty. Even if the *Ramsay* principle of construction were to apply, to the extent that the circular movement of money had to be disregarded, the dispositions were still of foreign property, for the reasons set out earlier, and therefore outside the charge.

Associated operations

Mr Henderson QC, counsel for the Commissioner, submits as his fall-back position that the expression "disposition" in s.6(1)(c) has, by virtue of s.3(1), been enlarged to include "associated operations". These are defined in the Ordinance as

"(a) operations which affect the same property; or one of which affects some property and the other or others of which affect property which represents, whether directly or indirectly, that property ...; or

(b) any two operations of which one is effected with reference to the other, or with a view to enabling it to be effected or to facilitating its being effected, and any third operation having a like relation to either of those two, and any fourth operation having a like relation to any of those three, and so on,

whether those operations are effected by the same person or by different persons, whether they are connected otherwise than as aforesaid or not, and whether they are contemporaneous

or any of them precedes or follows any other."

Mr Henderson says that the Commissioner does not seek to use the concept of "associated operations" to alter the nature of the individual operations, but simply to identify the subject matter of the gifts that were made by the deceased, for estate duty purposes.

The concept of associated operations does not help the Commissioner. It begs the question as to what gifts were made on the relevant dates which attract estate duty under s.6(1)(c). The Commissioner is unable to state what were the *dispositions* by way of associated operations which could be categorised as immediate gifts of Hong Kong property on the relevant dates, and falls back ultimately on his *Ramsay* arguments. At the end of the day, the point concerning "associated operations" is nothing more than a boost to the main issue.

Conclusion

I would allow the appeal, discharge the orders of the Court of Appeal, and restore Findlay J's orders. As to costs, the appellants must have their costs here and below.

Mr Justice Bokhary PJ :

Each of these transactions include, in my view, intermediate steps artificially inserted for tax-avoidance purposes alone. Even so, merely disregarding those steps would not of itself bring the Commissioner of Estate Duty success under the *Ramsay* doctrine. The case which the Commissioner seeks to make out under the doctrine is ultimately dependent upon a radical re-characterisation of the end result of each of the transactions. In regard to the Manx transactions, releases by the deceased of debts situated in the Isle of Man would have to be re-characterised as gifts by him of Hong Kong property. In regard to the Macanese transaction, the gift by the deceased in Macau of sale proceeds which he had received there would have to be re-characterised as a gift by him of Hong Kong property. And all of that would have to be done in the absence of sham. In my view, none of the foregoing re-characterisation is possible under the *Ramsay* doctrine in its present state of development.

Certainly I do not deny that the *Ramsay* doctrine is capable of further development. In this regard I note and fully see the force of - Lord Steyn's statement in *IRC v. McGuckian* [1997] STC 907 at p.916g that "Given the reasoning underlying the new approach it is wrong to regard the decisions of the House of Lords since the *Ramsay* case as necessarily marking the limit of the law on tax avoidance schemes". And this finds a strong echo in Lord Cooke of Thorndon's statement in the same case (at p.921a) that "the journey's end may not yet have been found".

So it would appear that the *Ramsay* doctrine is quite capable of further development. But I would leave that to the House of Lords on some future occasion, which may well not be very long in coming, rather than take it up in the present appeal, which is the *Ramsay* doctrine's debut in this Court. In so saying, I am of course far from suggesting that nobody else's input could ever possibly be of value. Indeed the *Ramsay* doctrine appears to owe much to Judge Learned Hand of the United States Court of Appeals. This indebtedness was acknowledged by Lord Wilberforce in the *Ramsay* case itself, *W.T. Ramsay Ltd v. IRC* [1982] AC 300, where (at pp 326 H-A) his Lordship cites *Gilbert v. CIR* (1957) 248 F. 2d 399 at p.411. And it is perhaps worth mentioning that Judge Learned Hand's contribution to this area of the law is more fully dealt with by Mr Peter Millett QC (now Lord Millett) in his illuminating article

"Artificial Tax Avoidance. The English and American Approach" 1986 British Tax Review 327. (Having drawn attention to this article, I should mention for the convenience of readers that the case of *CIR v. Ickelheimer* is in fact reported at (1943) 132 F 2d 660 although the incomplete and incorrect reference "(1934)" is given to it at p.331 of the article.)

Despite what it owes to Judge Learned Hand, the *Ramsay* doctrine comes to us as a fairly recent creation or discovery of the House of Lords. I am not disposed to apply the doctrine in any way which lies beyond its present state of development at their Lordships' hands. And I do not see how the Commissioner can succeed unless the doctrine were applied in some such new way.

For the reasons which I have given and the reasons far more fully stated in Sir Anthony Mason NPJ's judgment, with which I agree on all matters including its rejection of the Commissioner's "quasi-sham" and "associated operations" arguments, I too would allow this appeal to make the orders announced by the Chief Justice. I do this with an expression of my thanks to counsel on both sides for their most helpful submissions.

Mr Justice Silke NPJ :

I have had the opportunity to read in draft the judgment of Sir Anthony Mason NPJ. I respectfully agree with its conclusions, the reasoning therefor and the orders proposed.

Sir Anthony Mason NPJ:

Introduction

The central issue in this appeal is whether certain dispositions, made in his lifetime by Pong Ten Un ("the deceased") who died on 23 January 1993, are to be treated for estate duty purposes as transfers, made by way of gift, of property situate in Hong Kong. The dispositions, which were made in the course of a complex series of transactions, were evidently made with the provisions of s.10 of the Estate Duty Ordinance, Cap.111, ("the Ordinance") in mind. The section provides :

"Estate duty shall not be payable in respect of -

...

(b) property situate outside Hong Kong."

As will appear, if, for estate duty purposes, full effect were to be given to the dispositions according to their form, no duty would be payable. That is because the dispositions effected a transfer of property situated in Hong Kong and its replacement either by specialty debts situated outside Hong Kong or by the proceeds of sale situated in Macau which were the subject of a gift made outside Hong Kong.

The respondent concedes that the transactions giving rise to the dispositions were not sham transactions in the ordinary sense of that expression but contends that, for estate duty purposes, full effect cannot be given to the dispositions according to their form. Three grounds are advanced in support of this contention. They are :

1. 1. that the principle in *Ramsay (W.T.) Ltd v. IRC* [1982] AC 300 applies with the result that certain transactions ("the intermediate transactions") are to be disregarded, leaving residual dispositions of property situated in Hong Kong;
2. 2. that the intermediate transactions, though not shams, were quasi-shams and were to be disregarded with consequences similar to those in (1); and
3. 3. that a number of the transactions fell within the "associated operations" provisions of the Ordinance, again with similar consequences.

The end result of each of these submissions, if successful, would be to establish, so the respondent's arguments run, that the dispositions are to be treated for estate duty purposes as transfers, made by way of gift, of property situated in Hong Kong and are dutiable as such.

The dispositions

The deceased disposed in his lifetime of shares which he held in a number of Hong Kong companies and of two real estate properties situated in Hong Kong, "the Hillview property" and "the YTIL property".

In December 1989, the first appellant ("SWL"), a Manx company incorporated on 18 December 1989, established in the Isle of Man, 5 unit trusts. These 5 unit trusts were the SW Steel Unit Trust, the SW Investments Unit Trust, the Mack Unit Trust, the Hillview Unit Trust, and the YTIL Unit Trust. The sole trustee of each of those unit trusts was SWL. The directors of SWL were the deceased's wife ("the mother") and his 7 children, Harry, Frank, David, Edward, Stanley, Elizabeth and Teresa. The sole shareholders in SWL were the second appellant ("Futurian") and the third appellant ("SKL"). The directors of Futurian were the mother, Stanley, Elizabeth and Teresa. The directors of SKL were Harry, Frank, David and Edward.

On 25 January 1990, the deceased made the following transfers of property to SWL : (1) 2,590,000 shares in Shiu Wing Steel Limited ("the SWSL shares") to SWL in its capacity as sole trustee of the SW Steel Unit Trust; (2) 65,800 shares in Shiu Wing Investments Limited ("the SWIL shares") to SWL in its capacity as sole trustee of the SW Investments Unit Trust; (3) 1,100 shares in Easiatic Warehouse and Forwarding Limited ("the EWFL shares") to SWL in its capacity as sole trustee of the SW Investments Unit Trust; (4) 4,700 shares in Mack & Co. (Freight Forwarders) Limited ("the Mack & Co. shares") to SWL in its capacity as sole trustee of the Mack Unit Trust; and (5) the Hillview property to SWL, in its capacity as trustee of the Hillview Unit Trust.

On 25 January 1990, the deceased as settlor made a transfer of HK\$42,200,000 by way of gift to the second plaintiff ("Futurian") and the third plaintiff ("SKL") in their capacity as joint trustees of a Manx trust known as the Pong Ding Yuen Trust. Futurian and SKL were the sole holders of units in the Unit Trusts (apart from one initial unit the Hillview Unit Trust issued to the mother). Futurian held units as sole trustee of four discretionary trusts constituted (it seems) primarily for the benefit of each of four of the deceased's children. SKL held units as sole trustee of three discretionary trusts constituted (it seems) primarily for the benefit of each of the remaining three children.

The transfers of shares and of the Hillview property constituted the first steps in a series of composite transactions effected in Macau. Contemporaneous steps in this series of transactions were the provision of consideration for the transfers of property already

mentioned. This consideration was provided as follows :-

1. 1. the mother borrowed \$139,000,000 by way of unsecured loan from a bank;
2. 2. she lent the money (other than that required for the YTIL transaction) to SWL in its capacity as sole trustee of the Unit Trusts;
3. 3. SWL used part of the money to provide consideration for the transfer by the deceased to SWL of the SWSL shares, the SWIL shares, the Easiatic shares, the Mack & Co. shares, and the Hillview property; SWL used the balance of the money to acquire from the deceased's children shares held by them in the same companies;
4. 4. the deceased then lent the money representing the consideration for the shares to Futurian and SKL in their several capacities as sole trustees of the 7 children's trusts mentioned above, the loans giving rise to specialty debts owing to him, the debts being repayable on demand, free of interest, without security and the right of repayment being personal to the deceased;
5. 5. the deceased then transferred \$42,200,000 (being the consideration for the Hillview property) by way of gift to Futurian and SKL in their capacity as joint trustees of the Pong Ding Yuen Trust;
6. 6. Futurian and SKL then used the money to pay SWL for units in the 5 unit trusts;
7. 7. SWL then used the money to repay the mother the money which the mother had earlier transferred to it;
8. 8. the mother then repaid the money to the bank.

The money used to finance these transactions was provided, in the beginning, by the bank to the mother, and, in the end, returned by the mother to the bank. Each set of transactions was financed by circular movements of money, each one of which took the following route; bank to mother; mother to SWL; SWL to deceased (or child); deceased or child to Futurian or SKL; Futurian or SKL to SWL; SWL to mother; and mother to bank.

The amount of \$139,000,000 included the amount necessary to complete the YTIL transaction which may have been planned initially to take place on 25 January. \$139,000,000 was not the total of the loans made by the mother. The total amount of the loans made by her on 25 January was \$255,976,228. However, as each loan was repaid to the mother on that day, before the next loan was made, the amount actually needed to finance the transactions on that day was \$42,200,000. The balance of the \$139,000,000 was the amount required for the YTIL transaction.

On 25 January 1990, the deceased made a Manx will expressed to forgive at his death all debts owed to him by Futurian or SKL.

On 24 October 1990, the steps taken on 25 January 1990 in relation to the transfers of shares effected on that day were replicated in respect of the YTIL property.

On 24 October 1991, the deceased, anticipating what he had done by his will of 25 January 1990, released by deed inter vivos the debts owed to him by Futurian and SKL as a result of the 25 January 1990 transactions, and, on 22 October 1992, he did the same in respect of the debts owed to him as a result of the 24 October 1990 transactions.

The end result of all the transactions was that the assets the subject of the transfers continued

to be situated in Hong Kong until the deceased's death. But they were no longer owned by the deceased; instead they were held ultimately for the benefit of his family through the Isle of Man trust structure.

The proceedings in the High Court

The appellants sought a declaration in the High Court that no estate duty is payable in respect of the property which was the subject of the transfers. Findlay J. granted the declaration sought. The respondent was ordered to pay the appellants' costs.

Before Findlay J., and later in the Court of Appeal, argument centred upon the *Ramsay* principle, namely that where there is a composite transaction into which steps have been inserted that have no business purpose other than tax avoidance, the inserted steps may be disregarded for tax purposes and the charging provisions applied to "the end result".

Having regard to the view which he formed of the purpose of the transactions, Findlay J. concluded that the case did not fall within the *Ramsay* principle. This conclusion followed, first, from a finding that there were non-fiscal as well as fiscal reasons for the composite transaction or scheme and the fact, conceded by Senior Counsel for the respondent, that there were non-fiscal purposes for the transfer of the Hong Kong property offshore, the establishment of the trusts and the issue of the units. His Lordship also concluded that it was not a legitimate application of the *Ramsay* principle to reconstruct the transactions in a series by picking bits out and by rejecting other bits. Accordingly it was not possible to hold that there were dispositions of property within s.6(1)(c) in accordance with the *Ramsay* principle. His Lordship went on to reject the respondent's submission that certain transactions were shams and the "associated operations" argument.

Although the learned judge referred to the overall transactions as "the composite transaction", it is common ground that each of the six transactions should be treated as a "composite transaction" for the purpose of the *Ramsay* principle, if the requirements of the principle in that respect are otherwise satisfied.

The Court of Appeal

The Court of Appeal (Mortimer V-P, and Godfrey JA, with Rogers JA dissenting) allowed the respondent's appeal from the declaration made by Findlay J. and ordered that the appellants should pay the respondent's costs of the appeal and of the proceedings in the High Court. In essence, the majority considered that there was no good non-fiscal purpose for the intermediate steps in the composite transaction. In this respect, their Lordships appear to have taken the view that there was one overall composite transaction, though it is possible that they regarded the YTIL transaction as a composite transaction in its own right.

Nor is it clear what the majority understood to be "the intermediate steps". It may well be that their Lordships had in mind the pre-ordained transactions of the bank loan to the mother, the loans by the mother to the unit trusts, the sales of property, followed by the gift (in the case of the Hillview property) or the loan (in the case of the other properties) of the proceeds of sale to the trustees of the discretionary trusts, the subscription for units in the discretionary trusts, the repayment of the loan by the mother, the creation of the specialty debts and the execution of the Manx will forgiving the debts. It is these transactions which, on the respondent's case, constitute the intermediate steps which are to be disregarded. The

respondent does not challenge the validity or the commercial reality of the Isle of Man trust structure.

On the other hand, Rogers JA considered that there were viable non-fiscal reasons for all the steps which were taken in the six transactions. On this view, there were no intermediate steps. His Lordship also held that the forgiving of the specialty debts was not pre-ordained. Accordingly, the *Ramsay* principle had no application. Rogers JA then went on to reject, as had the primary judge, the two alternative arguments advanced by the respondent, holding that the relevant transactions were not shams and that the forgiveness of the loans in 1991 did not amount to an "associated operation" within the meaning of that expression as defined in s.3 of the Ordinance.

The statutory provisions

It is convenient now to refer to the relevant provisions of the Ordinance (other than s.10(b)).

Section 5 states that estate duty is payable on the value "of all property passing on death ..."

Section 6 provides that :-

"(1) Property passing on the death of the deceased shall be deemed to include the property following -

(c) ... taken under a disposition made by him, purporting to operate as an immediate gift inter vivos, whether by way of transfer, delivery, declaration of trust, or otherwise, which shall not have been bona fide made 3 years before the death ..."

Property includes both movable and immovable property (s.3). "Disposition" is defined by s.3 as including :

"any trust, covenant, agreement or arrangement, whether made by a single operation or by associated operations, ..."

Section 3 also defines "associated operations" as meaning :

"any 2 or more operations of any kind being -

(a) operations which affect the same property, or one of which effects some property and the other or others of which affect property which represents, whether directly or indirectly, that property or income arising from that property, or any property representing accumulations of any such income; or

(b) any 2 operations of which one is effected with reference to the other, or with a view to enabling it to be effected or to facilitating its being effected, and any third operation having a like relation to either of those two, and any fourth operation having a like relation to any of those three, and so on,

whether those operations are effected by the same person or by different persons, whether they are connected otherwise than as aforesaid or not, and whether they are contemporaneous or any of them precedes or follows any other;"

The facts

It was common ground, at least in the Court of Appeal and in this Court, that the deceased had a number of good reasons for transferring the property in question out of the jurisdiction. There was uncertainty as to the future of the commercial operations in Hong Kong of SWS. In October 1985, a competitor's premises at Junk Bay had been resumed by the Government and in May 1988 the Government informed the Company that its steel mill at Junk Bay was incompatible with the development of the new town. The possibility of re-location to Tuen Mun was considered.

It was thought that it might be advantageous to commence operations in Canada. In that event, it was doubted that a Hong Kong company would be a suitable investment entity. Then there was uncertainty over the future of Hong Kong itself, including the political and economic risks (involving possible exchange control measures) arising from the resumption in 1997 by the People's Republic of China, of the exercise of sovereignty over Hong Kong. The members of the Pong family were advised that if family members were to move to Canada, it would be desirable to have their assets already in an off-shore non-resident trust or company before they established residence in Canada in order to avoid liability to Canadian tax.

These factors, which were significant, indicated that there was a need for the deceased and his family to take steps to protect the assets. This need became the greater in 1990 when the deceased was 85 years old and suffering from cancer. The taking of estate planning measures to avoid or reduce the incidence of estate duty on his death then became an important consideration.

It follows that the reasons or motives which induced the deceased to set in train the complex of transactions, viewed as a whole, were partly fiscal and partly non-fiscal. Whether the same reasons or motives induced the deceased to set in train what have been called "the intermediate transactions" is a matter of dispute. In this respect, it is important to note that the *Ramsay* principle is concerned with the purpose of a transaction - the aim or end in view - rather than with the motives or reasons which induce the party to enter into it, or with the effect of the transaction. That said, the motives or reasons for entering into a transaction, though never decisive may, in some situations, throw some light upon the purpose of the transaction.

The Ramsay issues

The appellants' case begins with the proposition that, on 25 January 1990, the deceased converted his Hong Kong shares into foreign property i.e. the specialty debts. This he did by selling the Hong Kong property to the Isle of Man Unit Trusts for a full market consideration, by lending the proceeds of sale to the trustees of the seven Isle of Man discretionary trusts for the benefit of his family (the debts being specialty debts situated outside Hong Kong) and by the trustees using the money lent to subscribe for units in the Unit Trust. There was no gift of property. This proposition embraces the share transactions and the later YTIL transaction, there being no material difference between them.

The appellants' next proposition is that the Hillview transactions on the same day again involved a conversion of Hong Kong property into foreign property i.e. the sale proceeds in Macau. The sale proceeds were then given to an Isle of Man discretionary trust, the Pong

Ding Yuen Trust. That was a gift but it was a gift of foreign property.

The respondent does not contest these two propositions. However, the respondent relies upon the *Ramsay* principle to bring about the result that in each of the above transactions there was a gift of property in Hong Kong. According to the respondent, the underlying substance or end result of the transactions was that the deceased made a gift of Hong Kong property, the gift being either a gift to SWL on condition that units of corresponding value would be issued to the trustees of the relevant discretionary trust or a gift to SWL with a discretion to issue the units.

The appellants contend that the *Ramsay* principle cannot achieve this result for two principal reasons. One is that the "no commercial purpose" test in *Ramsay* is not satisfied. The other is that, under the *Ramsay* principle it is the "end result" that falls to be taxed and the "end result" was not a gift of Hong Kong property.

The Ramsay principle

There are several preliminary comments to be made about the *Ramsay* principle. It is a principle which has attracted criticism largely but not entirely on the ground that it amounts to judicial legislation. In *IRC v. McGuckian* [1997] STC 908 at 915-916, Lord Steyn delivered a convincing riposte to this criticism (see also at 920 -921 per Lord Cooke of Thorndon). The principle accords with the basic legal principle applied in the courts of the United States to tax avoidance cases. In *Ramsay* at 326 - 327, Lord Wilberforce referred specifically and with evident approval to the judgment of Judge Learned Hand (dissenting on the facts) in *Gilbert v. Commissioner of Internal Revenue* (1957) 248 F.2d 399 at 411.

The principle is now well entrenched in English law. The principle has been accepted and applied in a long series of cases in the House of Lords, culminating in the decision in *IRC v. Willoughby* [1997] STC 995. In no case has the existence of the principle been denied by the House of Lords or by any Law Lord.

The principle, according to the House of Lords, is both a rule of statutory construction applicable to revenue statutes and an approach to the analysis of the facts. At first instance, Findlay J. had difficulty in seeing the principle as a rule of construction. His Lordship considered that it was in truth a way of viewing or, as I would express it, a way of analysing the facts. This element of the *Ramsay* principle may be expressed by saying that where there is a single pre-ordained, composite transaction intended to be carried out in its entirety, the court is not compelled for tax purposes to ignore its composite character and to break it up into its individual constituent steps so that the statute is then applied to those individual steps separately. If the purpose of intermediate steps in the composite transaction was fiscal they may be disregarded. The composite transaction may then have consequences which bring it within a charging provision of the statute.

As the House of Lords has said on a number of occasions, *Ramsay* is also a rule of construction. The point was well made by Judge Learned Hand in *Gilbert* to which reference has already been made. In that case (at 411), in a passage which includes that quoted by Lord Wilberforce in *Ramsay*, Judge Learned Hand expressed the purposive approach to statutory construction. This is what he had to say :

"It is a corollary of the universally accepted canon of interpretation that the literal meaning of

the words of a statute is seldom, if ever, the conclusive measure of its scope. Except in rare instances statutes are written in general terms and do not undertake to specify all the occasions that they are meant to cover; and their 'interpretation' demands the projection of their expressed purpose upon occasions, not present in the minds of those who enacted them. The Income Tax Act imposes liabilities upon taxpayers based upon their financial transactions, If, however, the taxpayer enters into a transaction that does not appreciably affect his beneficial interest except to reduce his tax, the law will disregard it; for we cannot suppose that it was part of the purpose of the Act to provide an escape from the liabilities it sought to impose."

Likewise, in *IRC v. McGuckian* [1997] STC 909, Lord Steyn noted (at 916) that the *Ramsay* principle,

"was not based on a linguistic analysis of the meaning of particular words in a statute. It was founded on a broad purposive interpretation, giving effect to the intention of Parliament."

See also at 920, per Lord Cooke of Thorndon.

There are to be found statements of high authority which acknowledge that Parliament intends that a taxpayer shall be free to place an asset out of the reach of the taxing provisions (*Craven v. White* [1989] AC 398 at 489, per Lord Templeman; *IRC v. Willoughby* [1997] STC 995 at 1004, per Lord Nolan). No doubt these statements will apply in situations in which a revenue statute, for particular policy reasons, offers tax exemptions, concessions and advantages for particular investments (see *Willoughby* at 1004, per Lord Nolan). This is not such a case. In any event, these statements must be read as being subject to the *Ramsay* principle.

It would be a mistake to regard the present formulation of the *Ramsay* principle as set in stone. Sufficient warning has been given that the existing formulation may not mark the end of the road (see *Furniss v. Dawson* [1984] AC 474 at 513, per Lord Scarman and 516-517, per Lord Bridge of Harwich; *IRC v. McGuckian* at 920-921, per Lord Cooke of Thorndon). That possibility is not, however, something to which we need to give attention in the present case, the parties having accepted that the principle forms part of the law of Hong Kong and that the central issue is to be resolved by the application of the principle as it presently stands on the cases.

The Ramsay principle and the present case

The classic statement of the *Ramsay* principle is to be found in *Furniss v. Dawson* [1984] AC 474. There Lord Brightman said at 527 :

"First, there must be a pre-ordained series of transactions, or, if one likes, one single composite transaction. This composite transaction may or may not include the achievement of a legitimate commercial (i.e. business) end ... Secondly, there must be steps inserted which have no commercial (business) purpose apart from the avoidance of a liability to tax. If those two ingredients exist, the inserted steps are to be disregarded for fiscal purposes. The court must then look at the end result. Precisely how the end result will be taxed will depend on the terms of the taxing statute sought to be applied."

For present purposes the principal significance of this statement lies in the second limb because it is common ground between the parties in this Court that there was a series of pre-ordained transactions, comprising six composite transactions. Of all the transactions which I have described only the deeds releasing the debts were not pre-ordained. As Mr Henderson

QC for the respondent submits, the second limb indicates that the *Ramsay* principle may apply even in circumstances where the composite transaction viewed as a whole achieves a legitimate non-fiscal purpose. Another point be made from the decision in *Furniss v. Dawson* itself, is that the principle is not confined in its application to self-cancelling transactions. It applies to linear transactions as well.

It follows that two principal questions arise in connection with the *Ramsay* principle, on the arguments presented by the parties. The first is whether the so-called "intermediate steps" were inserted without any purpose other than a tax advantage. The second is whether, if those steps can be properly disregarded, there is an "end result" which falls within the grasp of the Ordinance.

The intermediate steps

On the question whether each composite transaction contained steps which were inserted without any purpose other than tax avoidance (*Furniss* at 527), we do not have any finding of fact by the primary judge or by the Court of Appeal. The Ordinance contemplates that the Court of First Instance will decide questions of fact as well as questions of law (see s.22 which is not limited to appeals on questions of law). In the absence of findings of fact, by the courts below, it is open to this Court to draw inferences of fact from the materials before it. In the drawing of such inferences, the fact that the appellants were the moving parties in the proceedings, means that it was for them to give evidence of non-tax avoidance reasons, if any, for entering into the intermediate transactions, these being matters within their own knowledge.

With this in mind, I turn to the transactions. First, there is the extreme artificiality of the financial arrangements. One complete cycle of money movements from and back to the mother was used to finance each transaction in the series. The bank was repaid only when the series of transactions was completed. The bank simply presented a set of statements showing money movements. The lack of commercial reality in the loan is evidenced by the fact that it was unsecured and interest free which indicates that there was no commercial risk to the bank. And, as the respondent points out, no attempt was made to reduce the loan from \$139,000,000 to \$42,200,000 on 25 January when the YTIL transfer did not proceed on that day. To say, as Rogers JA suggested, that the bank lending is explicable by reference to the relationship between the mother and the bank is to draw a speculative inference which could readily have been established by evidence, if the inference was based in fact. Nor was the mother a beneficiary of the Pong Ding Yuen Trust. Rogers JA seemed to think she was. It matters not that the bank lending was valid (as Rogers JA thought it was) or genuine in the sense that it was not a sham lending. In this respect, all that *Ramsay* is concerned with is whether the purpose was solely fiscal.

Next, the Isle of Man trust structure was under close family control. Futurian and SKL, which were under family control, were the sole shareholders in the five Unit Trusts (apart from one initial unit in the Hillview Unit Trust held by the mother) and in SWL, the trustee of the Unit Trusts. The mother and the seven children made up the directors of Futurian and SKL.

It is instructive to look, first, at the Hillview transactions, where the deceased gave the proceeds of sale to Futurian and SKL as trustees of the Pong Ding Yuen Trust, and ask the question : what reason was there for entering into the intermediate transactions rather than

simply transferring the property to SWL by way of gift and procuring the issue of the relevant units by SWL to Futurian and SKL? The answer must be that the intermediate transactions were undertaken for the purpose of tax avoidance. A voluntary transfer of the property followed by the issue of the units would have satisfied the non-fiscal purpose of conferring benefits through the trusts on the members of the deceased's family, benefitting one's family being a non-fiscal purpose in the *Ramsay* context (see *Ingram v. IRC* [1997] STC 1234 at 1270, per Millett LJ (dissenting but not on this point)). But the adoption of this alternative would have resulted in a liability to estate duty had the deceased died within three years (see the Ordinance, s.6(1)(c)). In January 1990, the deceased, who was then 85 years old, had been suffering from cancer for about 5-6 years. The prospect of death within three years would clearly have been within his contemplation and that of his family.

The only inference as to purpose that can reasonably be drawn in these circumstances is that the Hillview intermediate transactions were undertaken simply to avoid estate duty by transforming what would have been a gift of property within the jurisdiction into a transfer of property for full consideration with the consequence that there would be a gift of the proceeds of sale outside the jurisdiction.

In reaching this conclusion, I have given consideration to the reasons given by Rogers JA for reaching the contrary conclusion. Those reasons turn largely on the proposition that the intermediate steps were necessary to effectuate the commercial purpose of housing the assets in an off-shore trust structure. Granted that motivation, it does not explain why the intermediate steps had to be taken to achieve that commercial purpose. The suggestion that transfers of property for full consideration rather than transfers by way of gift were implemented in order to create a better title is an unrealistic argument unsupported by any evidence.

An examination of the share transactions and the YTIL property transactions yields the same inference as to purpose as far as the intermediate steps are concerned. What reason was there for entering into them instead of simply transferring the property to SWL by way of gift and procuring the issue of the relevant units? Again, the answer would seem to be that the mother's loans, the sales of property, the repayment of the mother's loans, the loans by the deceased to Futurian and SKL as trustees of the discretionary trusts, the creation of the specialty debts and their forgiveness by the Manx will had only one purpose and that was the avoidance of the estate duty that would have been imposed had the deceased simply made a gift of the relevant property to the trustees for the benefit of the family.

Crucial to this conclusion is the purpose of the loans to the trustees of the discretionary trusts. The appellants rely on the evidence of Frank Pong, one of the deceased's children, that the deceased

"kept his options open to require payment of the loans"

That statement suggests that making the loans and keeping them on foot vested an ultimate sanction or control over the discretionary trusts in the deceased. He could call up the loans at any time. Frank Pong was not cross-examined on this statement. On the other hand, the loans were of great magnitude repayable on demand and free of interest. No trustee would wish to be burdened with such large loans, more particularly loans repayable on demand. That consideration indicates that the parties understood that the loans were not to be called up and

that they were to be forgiven, the Manx will making appropriate provision in that respect.

Accordingly, the purpose test is satisfied.

The end result

What then is the end result, once the intermediate steps are disregarded? And does it fall within the charging provisions of the Ordinance? The end result of a composite transaction is the residue which is left after the tax-driven intermediate steps are disregarded (*IRC v. McGuckian* [1997] STC 908 at 914, per Lord Browne-Wilkinson).

The appellants argue that Findlay J. was right in holding that the end result is that the deceased disposed of his Hong Kong property for full consideration and made a gift of units in the Isle of Man Unit Trusts i.e. a gift of foreign property. On the other hand, the respondent contends that this is an unrealistic view of the matter and that the true view of the end result is that the deceased, having Hong Kong property, gave it to his family. The respondent acknowledges that this broad generalisation involves an element of inaccuracy because it fails to take account of the holding by the family members through trustees of units in the Unit Trusts. So the respondent submits that the appropriate re-construction of the transactions for fiscal purposes is either :

- a. a. as a conditional gift of the Hong Kong property, that is, as a gift to SWL on condition that units of corresponding value were issued to the trustees of the relevant discretionary trusts; or
- b. b. as a gift to SWL coupled with a direction to SWL to issue the units.

The appellants respond by contending that this is an impermissible characterisation of the end result because it represents more than the residue which is left after disregarding the intermediate steps and because it represents an unrealistic characterisation of the substance of the transactions.

The respondent's case in support of the end result which it advances is largely based on the decision in *Furniss v. Dawson*. In that case, the House of Lords disregarded the transfer by the taxpayers of shares in the operating companies to the intermediary company Greenjacket Ltd and the transfer by that company of the shares to Wood Bastow Ltd and held that, for the purposes of the Finance Act 1965, there was a disposal by the taxpayers in favour of Wood Bastow in consideration of a sum of money paid with the concurrence of the taxpayers to Greenjacket. The disposal attracted capital gains tax. The end result was arrived at by disregarding the interposition of Greenjacket and by collapsing the two transactions into one disposal by the taxpayers to Wood Bastow. According to the respondent, *Furniss v. Dawson* shows that some degree of reconstitution of the residue is permissible.

Furniss v. Dawson was, however, a relatively simple case. There was a pre-existing informal agreement between the taxpayers and Wood Bastow for the sale of the shares in the operating companies to that company. Greenjacket was interposed as an intermediary company solely for tax avoidance purposes. Moreover, Greenjacket did not exercise control of the operating companies, a matter of significance in the application of the relevant statutory provisions.

Subsequently in *Countess Fitzwilliam v. IRC* [1993] STC 502, the House of Lords not only took a restricted view of what can be done by way of reconstitution of particular transactions

but also explained *Furniss v. Dawson* as a decision turning on its own particular facts. In *Countess Fitzwilliam*, the Crown ran into difficulties because it changed its course on appeal, conceding that an important first step previously alleged to have been part of a pre-ordained series of transactions was not part of that series. The Crown having argued that steps (2) to (5), though genuine, were pre-ordained and tax-driven, sought to reconstitute them in a form different from that which they actually took. Step (2) in the series was a gift of £2m made by Lady Fitzwilliam to Lady Hastings. Step (4) was an assignment by Lady Fitzwilliam, of her interest in certain income to Lady Hastings in consideration of £2m paid to her by Lady Hastings. The Crown sought to reconstitute the transactions by characterising the gift as conditional and the assignment as gratuitous.

Lord Keith of Kinkel, speaking for the majority, had this to say of the argument (at 514 - 515) :

"Although the commissioners found as a fact that Lady Hastings accepted the £2m as a genuine unconditional gift from her mother, the Crown's case seeks to make it a conditional gift. Further, although all the transactions were accepted by the commissioners as genuine, the Crown's case seeks to make out that step 4 was not an assignment for a consideration but a gratuitous assignment. No case applying the Ramsay principle has yet held it to be legitimate to alter the character of a particular transaction in a series or to pick bits out of it and reject other bits. In *Furniss v. Dawson* the transfer to the intermediary company Greenjacket was disregarded for fiscal purposes because of the pre-existing informal agreement and of the manner in which the two transactions were carried out, which made it intellectually possible to hold that Greenjacket never had control of the operating companies within the meaning of the statute. No comparable exercise is possible here." (my emphasis)

The significance of the passage just quoted lies in the fact that the majority in the House of Lords proceeded on the footing that steps (2) and (4) were genuine (i.e. "non-sham") transactions, though forming part of a series of transactions which were pre-ordained in the sense that they all formed part of a pre-planned tax avoidance scheme. It followed that it would have been possible to disregard steps (2) and (4), along with other intermediate steps, for the purpose of the *Ramsay* principle. But it was not possible, in disregarding them, to give them another character. Or, to put it another way, having disregarded steps (2) and (4), it was not permissible to re-constitute the entire transactions by giving these two transactions a character different from their genuine character.

The reference to *Furniss v. Dawson* is also important because it shows that the existence of the informal agreement enabled the House of Lords to characterise the end result as a disposal to Wood Bastow. The inference is that, absent such an agreement and the manner in which the two transactions were carried out, it would not have been possible to characterise the end result so that duty was chargeable. There was in *Furniss v. Dawson* the additional problem of double taxation. It was the existence of this problem that led Lord Oliver of Aylmerton to say in *Craven v. White* [1989] AC 398 at 512 :

"... it was basic to the analysis which produced the result in *Furniss v. Dawson* not simply that the intermediate step was effected with the sole purpose of procuring a tax advantage but that it could legitimately be treated, on the facts, as part of a tripartite contract, for it was only by such an analysis that the single composite transaction would be constructed and the suggested consequence of the double taxation on the same gain overcome."

The concept of a tri-partite contract was called upon in *Furniss v. Dawson* to justify the characterisation of the transaction by the House of Lords. One can understand why resort to

the concept was thought to be necessary in the circumstances of the case which included the double taxation problem. But that does not mean the existence of such a contract is required in all cases before the *Ramsay* principle can apply. But it may mean that it is not possible to bring some cases within the reach of the principle without resort to such a contract.

In my view, the present case is an illustration of a similar class of case. The reconstitution for which the respondent contends involves not simply ignoring or disregarding artificial transactions which were purely tax-driven but reconstructing what is left by converting transfers of property for value into transfers by way of gift, either absolute or conditional, and, if absolute, coupled with a direction by the deceased to the trustee of the Unit Trusts to issue units to the discretionary trusts. This would amount to a reconstruction of a kind that has not taken place in any case to which the *Ramsay* principle has hitherto been applied. It would involve attributing to the transfers a character (by way of absolute or conditional gift) which is different from the character which they had. There is in the evidence nothing in the way of an underlying agreement or understanding which supports such a reconstitution.

There is an additional problem in undertaking the reconstitution which the respondent proposes. It has been said in the cases that the reconstitution must be one which is "realistic" and "intellectually possible" (*Craven v. White* at 509, 512, per Lord Oliver of Aylmerton; *Countess Fitzwilliam v. IRC* at 513, per Lord Keith of Kinkel). In considering whether these requirements are satisfied, it is necessary to bear in mind that *Ramsay* merely "enables the courts to arrive at a conclusion which corresponds with the parties' intentions" (*Craven v. White* at 514, per Lord Oliver of Aylmerton).

In this respect, a conditional transfer or gift would be quite foreign to what was intended. Absolute transfers of property were central to the plan that was implemented and to the underlying intention of the deceased. The respondent's reconstruction would also involve, on the other approach, the giving of a direction by the deceased for the issue of the units. There is nothing in the evidence which supports the existence of an intention to give such a direction.

Viewing the six transactions from a broader perspective, after disregarding the intermediate steps, the most realistic reconstitution of the transactions and the one which comes closest to the underlying intentions of the parties is that there was a transfer of Hong Kong property to the SWL trustee of the Unit Trust in consideration of the trustee issuing units to the discretionary trust. That is the reconstitution which the appellants advance, on the assumption that their other arguments fail. It is a reconstitution which more closely accords with what happened and the parties' intentions than the more radical reconstruction advanced by the respondent (see *Piggott v. Staines Investments Co Ltd* [1995] STC 114 (where a more radical and more artificial reconstruction was rejected by Knox J)). It is also a reconstruction which is capable of satisfying the concept of a tripartite contract by which the deceased undertakes to the Unit Trust and the discretionary trusts that he will transfer the Hong Kong property to the Unit Trust in consideration of the Unit Trust issuing units to the relevant discretionary trusts. See again *Piggott v. Staines Investments Co Ltd* at 141 (where Knox J. considered that, in order to bring the end result within the *Ramsay* principle, it is necessary to formulate a contractual framework to bring the series of transactions into a single composite whole).

The end results in the present case

It is necessary to look at the particular transactions in the light of the general observations

which I have made.

(a) The Hillview property transaction

If the intermediate steps, identified by Mr Henderson QC for the respondent, are disregarded, we are left with a vesting of the property in SWL, the trustee of the Isle of Man Unit Trusts, which holds it for the ultimate benefit of the unit holders, the members of the deceased's family. Although the transfer was expressed to be for full consideration and was for full consideration, on the assumption that the intermediate steps, though disregarded, are genuine, the respondent's argument is that the transfer is to be treated as a transfer by way of gift.

This is the Crown's argument on the assignment in *Countess Fitzwilliam* which failed. It must also fail here. There is the distinction that here the argument relates to a disposition which is not an intermediate step and is therefore not to be disregarded. But that, it seems to me, if anything, raises the hurdle to an even higher level.

The respondent submits that the decision in *IRC v. McGuckian* sanctions a more liberal approach to the reconstitution of a transaction after intermediate steps have been disregarded. In that case, the taxpayer and his wife implemented a scheme which had the twofold purpose of converting dividend income into capital and of reducing the value of shares held by the taxpayer in a company, thereby minimising his exposure to a wealth tax. Pursuant to the scheme, the taxpayer and his wife transferred their shares in B Ltd to a non-resident settlement, the trustee of which was a Guernsey-resident company.

The beneficiaries were the taxpayer and his wife and the income was payable to the wife. In November 1979 B Ltd had income available for distribution amounting to Ir£400,055. On 23 November 1979 the trustee assigned the right to any dividend payable by B Ltd in 1979 to M, a United Kingdom-resident company associated with the parties' tax consultant, for Ir£396,054. On 27 November 1979 B Ltd declared a dividend of Ir£400,055 and gave a cheque for that amount to a solicitor for M Ltd. The solicitor paid the cheque into his client account, out of which he then paid 99% of that sum (Ir£396,054) to the trustee, and the balance of 1%, less his own fee, to an agent for M Ltd.

The House of Lords held that, in the light of the genesis of the composite transaction in the mind of the tax consultant, the only possible inference was that the assignment of the right to the dividend by the trustee had been inserted for the sole purpose of gaining a tax advantage. The liability for tax on the indirect receipt of the dividend by the trustee had therefore to be determined by disregarding the assignment of the right to the dividend and applying s.478 of the Income and Corporation Taxes Act 1970 to the real transaction, the payment of the dividend to the trustee which received the dividend as income. Further, since the assignment had to be disregarded, s.470 of the 1970 Act did not apply and the income was not deemed to be income of the taxpayer's wife.

In treating the payment of the dividend by B Ltd to the solicitor for M Ltd and the subsequent payment by the solicitor of the lesser amount to the trustee as the payment of the dividend, the House of Lords ignored the assignment and re-characterised the payment to the trustee in the light of disregarding the assignment of the right to receive the dividend. But that does not involve re-characterising a legal disposition so that it is transformed from its genuine character to something else. This was the view rightly taken of *McGuckian* by Hart J in *DTE*

Financial Services Ltd v. Wilson [1999] STC 1061.

The re-constitution of the transfer is not the only problem in bringing the Hillview transaction within the grasp of the *Ramsay* principle. There is also a difficulty in re-constituting the unit trusts. If the loans and the payment of the proceeds of the sale of the Hillview property are to be disregarded, on what basis were the units in the five unit trusts issued by SWL to Futurian and SKL? They were paid for by Futurian and SKL out of the consideration for the Hillview property (which the deceased gave to Futurian and SKL). The respondent submits that the gift of the Hillview property is to be treated as a conditional gift i.e. as a gift to Futurian and SKL conditional on the issue of the units or as an absolute gift coupled with a direction to issue the units. To add either of these elements to the transactions is, in my view, impermissible and would fail to accord with the underlying intention of the parties for the reasons given earlier.

The shares and the YTIL property transaction

The essential difference in these transactions, when they are compared with the Hillview property transaction, is that the deceased lent the consideration for the transfers to the trustees of the unit trusts, the loans becoming specialty debts which were subsequently forgiven. But the difference does not remove the basic problem of re-constituting a transfer of property for full consideration as a transfer of property by way of gift. And, again it is necessary to assign a new legal basis for the transactions i.e. a conditional gift or a gift coupled with a direction to the trustees to issue units.

Accordingly, the six transactions fall outside the reach of the *Ramsay* principle.

The quasi-sham argument

This submission by the respondent was based on the observations of Lord Goff of Chieveley in *Ensign Tankers Ltd v. Stokes* [1992] 1 AC 655 at 681 where his Lordship, eschewing the use of the word "sham" in its orthodox sense, concluded that the "loans" were not loans in any meaningful sense and could only be characterised as steps in a tax-avoidance scheme. His Lordship then treated the loans as having no legal effect. Neither in *Ensign Tankers* nor elsewhere is there support for his Lordship's novel conception of a sham transaction. The conception cannot be equated to any of the steps in the *Ramsay* principle because that principle does not treat intermediate steps, which are disregarded for tax purposes, as having no legal effect.

For my part, I do not accept that his Lordship's approach should be adopted and I do not consider that, if adopted in this case, it would achieve more than the *Ramsay* principle would achieve.

Associated operations

The definition of "associated operations" enables separate transactions and dispositions to be aggregated for estate duty purposes. The definition is not, however, associated with any wider-ranging charging provision. Ultimately, in this case, it is a matter of applying s.6(1)(c) to a disposition, the meaning of which is enlarged by the inclusion of "associated operations". In the circumstances of this case, given that "associated operations" has an aggregating

effect, the respondent's argument cannot succeed if the *Ramsay* argument fails.

Conclusion

It follows that the appeal must be allowed. The orders to be made are as follows :

1. 1. Allow the appeal.
2. 2. Discharge the orders made by the Court of Appeal.
3. 3. Restore Findlay J's orders.
4. 4. The appellant must have their costs here and below.

Chief Justice Li :

The Court, being unanimous, makes the orders set out in the conclusion to the judgment of Sir Anthony Mason NPJ.