SECOND DIVISION, INNER HOUSE, COURT OF SESSION

[2020] CSIH 73
XA136/19

Lord Justice Clerk
Lord Woolman
Lord Pentland

OPINION OF THE COURT

delivered by LORD WOOLMAN

in the Appeal by Stated Case

by

NEIL CUNNINGHAM

Appellant

against

NAMULAS PENSION TRUSTEES LIMITED

Respondent

Appellant: Byrne; DAC Beachcroft Scotland LLP
Respondent: Reid; CMS Cameron McKenna Nabarro Olswang LLP

18 December 2020

Overview

[1] Mr Cunningham is a qualified solicitor and chartered accountant. At various times he has been a partner, director, or owner of several firms and businesses, including Kerslands LLP, solicitors; Kersco (WGS) Limited; Stafford & Clark; KS2013 LLP; Kerslands Solicitors Limited; and Mayfield (Edinburgh) Limited ("Mayfield").

[2] Mr Cunningham is the beneficiary of a self-invested personal pension plan ("the SIPP"). Until 2015 the SIPP owned a half share in two properties in the west end of Edinburgh. They comprised a terraced building at 12 Stafford Street, and a garage at 8 William Street Lane North East (respectively "No 12", "the garage" and together "the properties"). The purpose of a SIPP is to provide a tax exempt "wrapper" within which certain permitted types of investments, such as shares and bonds, may be held. Property and land may also be legitimately held, but not most types of residential property. For the purposes of the present case it is important to note that if a property held in a SIPP is converted from commercial to residential use, a tax charge will be imposed on the SIPP.

[3] Namulas Pension Trustees Limited ("Namulas") was the trustee of the SIPP. It was also the trustee of a different SIPP, which owned the other half share of the properties. The beneficiary of that SIPP was a "Mr E".

[4] The properties were used for commercial purposes for over a decade. From 2013 onwards Mr and Mrs S resided in No 12, having converted it for residential use. In 2015 they faced eviction proceedings raised in the name of Namulas. As part of an extra-judicial settlement it conveyed the properties to the couple in autumn 2015. Before the date of entry, the City of Edinburgh Council ("CEC") issued a completion certificate for the conversion works. As a result the SIPP incurred a significant tax liability because the property was considered to have become residential.

[5] Mr Cunningham attributed the diminution in the SIPP's value to Namulas. In early 2016 he lodged a complaint of maladministration with the Pensions Ombudsman ("PO"). He claimed that, in breach of its fiduciary duty to him, Namulas had failed to prevent the tax liability arising. It had also sold the properties at an under-value.

[6] The Deputy Pensions Ombudsman ("DPO") conducted the investigation into the complaint. She issued a preliminary decision in early 2018 indicating that she was not minded to uphold it. Later the same year, Mr Cunningham raised a court action against Namulas claiming damages for negligence. At the same time he wrote a letter withdrawing his complaint. The DPO, however, continued her work and issued a final determination in early 2019. It affirmed her preliminary view.

[7] Mr Cunningham now appeals to this court. There are two key issues. (1) Was the final determination legally flawed? (2) Should the DPO have allowed the complaint to be withdrawn?

Background

[8] A trust deed and rules governed the SIPP. It conferred wide powers on Namulas in its administration of the scheme. It could (i) delegate; (ii) appoint advisers; (iii) instigate and defend legal proceedings; (iv) settle or compromise claims; and (v) dispose of the trust assets.

[9] In 2002 Namulas appointed Mr Cunningham and Mr E to be the joint managing agents for the properties. The parties signed a property management agreement ("PMA") for that purpose. In the same year Mr Cunningham and Mr E arranged for Mayfield to take a commercial lease of the properties. It paid rent to both SIPPs.

[10] In 2011 Mayfield granted a licence to occupy the properties to Kerslands LLP. Mr Cunningham signed the document setting out the agreement on behalf of both parties. Mr E signed it on behalf of Namulas. Under its terms (i) Kerslands paid a licence fee as directed by Mayfield; (ii) Kerslands could grant sub-licences to third parties; (iii) the third

parties in turn could grant sub-sub licences if so approved by Kerslands; and (iv) the various occupancy regimes were designed to be terminable on 7 days' notice.

[11] Mr S owned the Period House Development Company Limited ("Period House"). He expressed an interest in purchasing the properties. He entered into negotiations with Mr Cunningham. They ripened into a provisional agreement. On 24 September 2012 Mr Cunningham wrote to Mr S (with a copy to Mr E) as follows:

> "You and I have agreed the outline of a deal (£490k for the office – with £30k of that deferred until you can release it from your site … and £85k for the garage) but, as discussed, that is subject to Namulas' approval. …
>
> Presumably you will need to get a change of use to resi?"

[12] The reference to "resi" plainly indicates the nature of the intended occupation of No 12. Matters proceeded on that basis. Toward the end of 2012 architects lodged a planning application for No 12 on behalf of Period House. They proposed a change of use from "office space to residential". CEC approved the application on 20 February 2013.

[13] Works at No 12 continued in the spring of 2013. The architects lodged another planning application to install a rear exit to comply with the fire regulations. They stated that the current or most recent use of No 12 was "residential". CEC approved the necessary works on 9 August 2013.

[14] Mr and Mrs S had begun living in No 12 in about May 2013.

[15] Other relevant events took place in 2013. In January 2013 Mayfield was dissolved. On 1 May 2013: (a) Kerslands changed its name to KS2013 LLP, (b) the new entity assigned the licence to occupy the properties to Kerslands Solicitors Limited, and (c) it in turn granted a sub-licence to Period House and Mr and Mrs S. Mr E signed the relevant documents on behalf of Namulas. Mr Cunningham signed them on behalf of KS2013 LLP and Kerslands Solicitors Limited.

[16] Several months later Mr Cunningham signed another important document on behalf of Kersco (WGS) Limited. It was a Short Assured Tenancy ("SAT") dated 29 January 2014, granting a lease of the properties to Mr S. The period of let was 1 February 2014 until 31 January 2015. The rent was £1,450 per month.

[17] The SAT agreement was both significant and curious. Significant, because it granted a degree of security to Mr S under section 32 of the Housing (Scotland) Act 1988. Curious, because Mr Cunningham later denied that Mr S (and through him Mrs S) had a valid right of occupation.

[18] Two weeks later, the properties became liable for council tax, rather than business rates. Around this time (early 2014), Namulas sent three emails to Mr Cunningham. It asked him to clarify the occupancy situation, given that Mayfield had been dissolved. He did not reply.

[19] On 2 July 2014 Mr S wrote to Mr Cunningham:

> "... I need a lease for [No 12], back dated from January, showing a rental but stating that this rent is not paid until mortgage comes through or until sale completes. Is that possible?
>
> I don't know what else to do here. As above the lending/mortgage market is being tightened. This regulated/unregulated 'thing' is also a factor as I live here."

[20] Two days later Mr Cunningham signed a declaration of trust between Kerslands Nominees Limited and Mr S. It showed that the shares in relation to Kersco (WGS) Limited were held by Kerslands Nominees Limited on trust for Mr S as the beneficiary. Mr S paid a non-refundable deposit of £42,000 to Stafford and Clark. This was paid by instalments into the SIPP with the reference "Mayfield".

[21] The precise effect of these documents does not matter. Their significance lies in showing that an intricate legal web surrounded the properties.

[22] On 16 December 2014, Kerslands Solicitors Ltd served a notice terminating its licence of the properties on Namulas. It was signed by Mr Cunningham and by Mr E on behalf of the respective parties. Its effect on the SAT was therefore uncertain, but Mr and Mrs S understood that their right of occupation was under threat.

[23] Solicitors acting on behalf of Mr and Mrs S wrote to Mr E on 18 December querying whether Namulas had approved the notice. They also stated that Mr and Mrs S had resided in No 12 for some time and were interested in purchasing the properties. This proposal did not find favour. Acting on Mr E's instructions, Harper Macleod, solicitors, initiated eviction proceedings.

[24] Namulas was not aware of these developments until the beginning of March 2015, when Mr and Mrs S made contact to say that (a) they had resided in the properties for over a year; (b) an action to evict them had been raised against them in its name; and (c) they would counterclaim for the rent already paid (*c* £40,000), and the cost of converting No 12 to residential use (*c* £175,000).

[25] On 4 March Namulas contacted Mr E, who described the situation as a "mess". On the same date it instructed Eversheds, solicitors, to take control of the action from Harper Macleod.

[26] The eviction proceedings took place over five months in 2015:

6 March	case continued for 7 days
13 March	case continued for 7 days
20 March	the sheriff ordered detailed pleadings and fixed a debate
28 April	a different sheriff assigned a 6 day proof to begin on 26 August
26 August	the parties reached an extra judicial settlement

[27] The common aim of the parties on the "landlord side" of the litigation was to secure eviction. Eversheds' advice was that Mr and Mrs S had no right to remain in the properties. It provided copies of the pleadings to Mr Cunningham to facilitate agreement on the litigation strategy. There was, however, a degree of disharmony. Namulas believed that the PMA had not allowed an action to be raised in its name. As early as 7 March, Mr Cunningham was critical of Namulas' approach.

[28] With the agreement of Mr Cunningham and Mr E, Namulas appointed DTZ, surveyors, to value the properties. After an inspection, DTZ provided a report dated 31 July with the following valuations (the figures in brackets are respectively for No 12 and the garage):

(a) current residential use with vacant possession – £760,000 (£675,000 + £85,000)

(b) commercial use in early 2013 – £630,000 (£550,000 + £80,000).

[29] Eversheds provided further advice to Namulas on 12 August. It stated that (a) the eviction proceedings carried a high degree of risk; (b) a negotiated settlement involving the sale of the properties to Mr and Mrs S would therefore be a "satisfactory outcome"; and (c) it was not practical to drop the action and allow the couple to remain in occupation until January 2016.

[30] Eversheds also wrote to Mr Cunningham along similar lines. Eviction "… carried a very high degree of risk and will require significant expenditure". The SIPP did not have funds to pay legal fees or other outgoings. Eversheds reminded Mr Cunningham that he had failed to answer several questions which they had previously posed, the answers to which might affect their view on the prospects of success in the action.

[31] Mr Cunningham and Mr E challenged Eversheds' advice. They asked the firm to clarify its logic and to complete a risk assessment schedule which they had prepared in relation to the action. Eversheds declined to do so.

[32] Mr Cunningham did not accept the DTZ figures. He instructed another firm of surveyors to carry out a "desktop" valuation. On 24 August (two days before the proof) the second firm said that No 12 should be valued at £750,000 and the garage at £100,000, but added that the DTZ valuation was "not wrong". This estimate was disclosed to Namulas.

[33] Settlement discussions intensified as the proof diet loomed. The sticking points related to the properties' value, the claimed licence fee arrears (also described as unpaid rent) and the legal fees. Over the course of the last week before the proof, there was a flurry of offers and counter offers:

19 August	*(At the suggestion of Mr M and Mr E)* Namulas offered to settle at £984,291.
25 August	Namulas rejected counter offers of £575,000 and £595,000.
26 August	Namulas proposed a figure of £650,000.
	Having initially refused to increase their offer above £595,000, Mr and Mrs S made an improved offer of £605,000.
	Namulas made a final offer of £610,000 (subject to ratification) which was agreed by Mr and Mrs S.

[34] The next day the board of Namulas ratified the settlement. The minutes of the meeting run to eight pages. They show that the directors considered the terms of the proposed extra-judicial agreement in light of the litigation risk, the legal advice, and the valuations.

[35] The settlement was unacceptable to Mr Cunningham. He instructed Namulas to transfer his SIPP immediately to an alternative provider. Namulas declined to do so. It

wished to notify HM Revenue & Customs to ascertain any tax liability before it transferred any funds.

[36] In the last quarter of 2015 three events took place: CEC issued a completion certificate for the No 12 building works (21 October), the properties were formally conveyed to Mr and Mrs S (19 November), and Namulas notified HMRC of the change to residential use (22 December). HMRC ultimately deemed the garage to be residential because its use was connected with the enjoyment of No 12.

The Complaint

[37] In early February 2016 Mr Cunningham lodged a complaint with the Pensions Ombudsman. He alleged that Namulas had breached the fiduciary duty it owed to him as the beneficiary. In particular, he contended that it had failed:

> (a) to prevent the properties becoming residential for tax purposes, resulting in an unauthorised payment tax charge (at a flat rate of 40%) and a surcharge;
> (b) to actively progress the court eviction process;
>
> (c) to sell the properties at an appropriate value; and
>
> (d) to transfer the SIPP to a new provider causing a proposed investment, namely the purchase of commercial property, to fall through.

[38] Mr Cunningham stated that the failures had disrupted his work, causing him to lose income of £175,000. He had also suffered distress and inconvenience. He queried the right of Namulas to charge advisers' fees to the SIPP to remedy what he contended were its own failures.

[39] In carrying out her investigation, the DPO exercised the same powers as the Ombudsman: section 145A of the Pension Schemes Act 1993 ("the 1993 Act"). She engaged in extensive correspondence with the parties. On 7 February 2018 she issued a preliminary decision, indicating that she proposed to reject the complaint. In her view Namulas had

properly and reasonably discharged its duty as the trustee of the SIPP. Accordingly there had been no maladministration.

[40] The DPO confirmed her decision in her final determination dated 11 January 2019. She held that Namulas had acted appropriately and on the basis of professional advice.

The challenge on the merits

[41] Mr Cunningham now brings this appeal by way of a stated case under section 151 of the 1993 Act and Rule 41.12 of the Rules of the Court of Session 1994. He asks this court to set aside the final determination. He contends that it is beset by legal error. Specifically, the DPO took into account immaterial considerations, ignored material considerations, and adopted an unreasonable view of the facts. We begin by outlining two distinct aspects of the legal framework.

[42] First, the complaint process. The Ombudsman may investigate and determine any complaint made by an individual who alleges that he or she "has sustained injustice in consequence of maladministration" by a trustee in respect of a pension scheme: section 146 of the 1993 Act. "Maladministration" is not defined, but counsel agreed it should receive a wide interpretation: *R* v *Local Commissioner, ex parte Bradford Metropolitan City Council* [1979] 1 QB 287 and *Mitre Pensions Ltd* v *Pensions Ombudsman* [2000] OPLR 349.

[43] Second, the tax regime. Happily we do not need to delve into the legislation. If a property held by a SIPP is converted or adapted to become residential, that is treated as if the scheme had made an unauthorised payment to a beneficiary: Finance Act 2004 section 174A(3). Such payments may be liable to a 40% flat rate of charge and a surcharge: sections 208 and 209. The key guidance is contained in the *Pensions Tax Manual ("PTM")* published by HM Commissioners of Customs & Excise. The relevant section states:

> ***"Property converted or adapted as residential property***
>
> The definition of residential property is a building or structure that is used or suitable for use as a dwelling. It does not therefore apply to property, including land, which is not residential property when the investment-regulated pension scheme acquires it. But the building or structure may become residential property whilst owned by the pension scheme as a result of being subsequently subject to development.
>
> Whilst it is in the course of construction, conversion or adaptation such land and property is not residential property because during that period it is not suitable for use as a dwelling.
>
> Land and buildings being converted are treated as residential property from the point when they become suitable for use as a dwelling.
>
> In any specific case this point should be determined by taking a common sense approach to the facts and circumstances.
>
> Essentially the question to be answered is: would a person normally live in that dwelling?
>
> The point at which this occurs will normally be when the works are substantially completed. In the case of UK property this is likely to be when the certificate of habitation is issued.
>
> A property that is sold before the development or conversion is substantially completed never becomes residential property."

[44] Mr Byrne submitted that the primary task of a SIPP trustee is to avoid triggering unnecessary and avoidable fiscal liabilities. Here the properties only became "residential" for tax purposes on 21 October 2015 when the completion certificate was issued. For the previous six months Namulas had sole control of the eviction proceedings. It ought to have done everything in its power to prevent or postpone the issue of the certificate. At the least it should have preserved a colourable argument with HMRC that the properties had not changed status. For example, Namulas could have notified CEC that it was the owner.

[45] According to Mr Byrne the DPO had misunderstood the complaint and failed to investigate it with sufficient rigour. She had trained her focus on events in early March 2015

and the eviction proceedings. Instead she ought to have considered the conduct of Namulas over the whole period.

[46] We reject Mr Byrne's submission. The DPO's reasoning is clear, detailed and cogent. In our view she conducted a comprehensive and thorough investigation into the complaint; she considered all the relevant issues and reached a rational result. We agree with her conclusion that it was reasonable for Namulas to take the stance that, by early March, the properties had been converted to residential use.

[47] A constellation of factors pointed in that direction. Mr and Mrs S had occupied the house for some time as their principal residence, having converted it at significant cost. They had a valid legal basis for their occupation, as Mr S was a tenant under the SAT. They paid council tax rather than commercial rates. Others formally involved with the properties, such as the architects and the local authority, also clearly thought that they were residential.

[48] The DPO was therefore entitled (and in our view correct) to hold that conversion did not arise as a result of some fault on the part of Namulas. She was entitled to proceed on the basis that it was reasonable for Namulas to assume that the Pensions Tax Manual test had been met. That squared with a common sense approach. Suppose in early March 2015 a third party had asked the question posed in paragraph 5 of the manual: would someone normally live at No 12? The obvious answer is "yes".

[49] The DPO was also entitled to have regard to Mr Cunningham's conduct. He did not provide answers to Eversheds' queries. He did not ask Namulas to take steps to prevent No 12 from becoming residential. Most significantly, the DPO posed a rhetorical question which we echo. If he did not consider No 12 to be residential, why did he sign the SAT?

[50] The other issues do not require lengthy analysis. The DPO was entitled to hold that Namulas acted reasonably:

(a) in reaching the extra-judicial settlement. Its directors carried out a thorough evaluation of the relevant factors at the board meeting;

(b) in refusing to transfer funds out of the SIPP until the potential tax liability had been ascertained and discharged.

[51] We therefore conclude that the DPO was entitled to hold that the complaint was unfounded. She understood the task at hand. We add a postscript. We do not accept that the issue of the certificate was determinative for tax purposes. While it provided the "long stop date", HMRC would have been perfectly entitled to conclude that the properties had become residential at a much earlier date.

Withdrawal of the complaint

[52] On 24 August 2018 Mr Cunningham wrote to tell the Ombudsman that the DPO "will no longer be dealing with my complaint". He explained that two days earlier he had raised an action seeking damages for negligence against Namulas in Dumbarton Sheriff Court.

[53] The DPO replied on 4 September stating that she had three options: (i) to grant leave to withdraw, (ii) to discontinue the investigation, or (iii) to make a final determination. She invited Mr Cunningham to make representations, but he chose not to do so.

[54] By contrast, the solicitors for Namulas urged the DPO to complete the complaint process. They contended that it would be a waste of time and resources for the issues to be re-litigated. They pointed out that Namulas had incurred legal fees of about £68,000. They also argued that a complainant should not be able to use the Ombudsman procedure as a "stalking horse" for a court action.

[55] Namulas enrolled to sist the court proceedings in terms of section 148 of the 1993 Act. It regulates the interface between the two resolution procedures. Plainly it would be

inappropriate for them both to run at the same time. That would carry the potential of the Ombudsman and the court reaching different factual findings. Section 148 confers a discretion on the court to sist the action if it is satisfied:

> (a) that there is no sufficient reason why the matter should not be investigated by the Pensions Ombudsman; and
>
> (b) that the applicant was at the time when the legal proceedings were commenced and still remains ready and willing to do all things necessary to the proper conduct of the investigation.

[56] On 25 September 2018 the sheriff sisted the court proceedings "to await the decision of the Pensions Ombudsman" in terms of section 148. It is important to note that Mr Cunningham did not oppose the motion.

[57] The DPO then continued work on the complaint until 28 November. On that date she desisted, because Harper Macleod informed her that Mr Cunningham had applied to recall the sist. On 4 December, however, the sheriff did not grant the recall motion. Instead he continued the hearing until 15 January 2019. At the same time he expressed a wish to see the complaint resolved prior to that date. That is what happened.

[58] Mr Byrne submitted that the letter of 24 August was an unequivocal request to withdraw. He accepted that it required "the leave of the Pensions Ombudsman which leave shall not be unreasonably refused": Rule 4 of the Personal and Occupational Pension Schemes (Pensions Ombudsman) (Procedure) Rules 1995.

[59] On his analysis the DPO either failed to make a decision on his request, or (if she did) she did not provide him with reasons for her refusal. In any event a refusal would be unreasonable, because he should not be required to continue in a process in which he had lost all faith. Each of these would constitute an error of law.

[60] We do not accept that Mr Cunningham made a clear and unequivocal request to withdraw his complaint. In the same letter he stated:

> "For the avoidance of doubt, my litigation against Namulas is without prejudice to my formal request of 20 August 2018 that Mr Arter, in his role as Pensions Ombudsman
>
> - Takes immediate steps to secure all letters, emails, file notes and other records relating to my complaints re Namulas …"

[61] That request, taken together with other factors, suggests that he adopted an ambivalent and unsatisfactory position in relation to the complaint. He did not engage with the DPO's request for representations. He did not oppose the sist. He sent various emails to the DPO about the substance of the complaint prior to the final determination. Accordingly, he gave every impression of continuing to participate in the complaint process.

[62] We acknowledge that Mr Cunningham did write to the Ombudsman on 18 September reiterating that he wished the court to resolve the dispute because of the manner in which (he contended) his complaint had been handled:

> "I think it is plain that the POS [Pension Ombudsman Service] has shown itself to be unable or unwilling to fulfil its statutory responsibilities in relation to my complaint about Namulas. I don't know what (if any) hold or influence Namulas has over POS and/or its personnel but I was forced to withdraw my complaint from POS because of its illegal acts, its multiple failures (including its repeated and ongoing contraventions of the principles of natural justice and fundamental errors in procedure) and what appeared to me to be its 'inherent bias in favour of Namulas'."

[63] Mr Cunningham wrote again on 15 December 2018 stating that the DPO should not reach a decision because it would be a legal "nullity".

[64] But even if the letter of 24 August can be seen as an unequivocal request to withdraw, it must have been plain to Mr Cunningham that the DPO had not granted him

leave to do so. She continued with the investigation until its completion and made him fully aware that she was doing so.

[65] Further, we conclude that it was reasonable for her to refuse to allow him to withdraw the complaint. The complaint was nearing a final determination. Namulas had incurred legal fees of about £68,000. The sheriff had indicated an expectation to see the conclusion of the complaint process, prior to the continued motion hearing on 15 January 2019.

Answers to the stated case

[66] We therefore answer the questions in the stated case as follows:

> 1. In proceeding to issue a Final Determination, did the DPO act unreasonably, or err in law, by either (a) failing to determine Mr Cunningham's application to withdraw his complaint; or (b) refusing, implicitly or explicitly, permission to withdraw his complaint? **No**
>
> 2. Did the DPO provide adequate reasons for the decision taken in respect of the application to withdraw the complaint? **Yes**
>
> 3 (a) Did the DPO err in law, have regard to an immaterial consideration or fail to have regard to a material consideration in determining whether there had been maladministration on the part of Namulas in administering Mr Cunningham's SIPP? (b) In particular, did the DPO adequately understand and address the complaint? (a) **No (b) Yes.**

[67] We refuse the appeal. In doing so, we acknowledge the assistance we derived from the concise and cogent submissions of both counsel.