



TAX LIABILITIES? CAN THE JERSEY COURT HELP?

OCTOBER 2018

The requirement to correct (RTC) notification deadline has now come and gone, and with it has surfaced some unexpected tax liabilities for trustees, settlors and beneficiaries.

For those facing a significant tax liability which has arisen as a result of a *genuine* mistake, and concerns a transfer into trust or an exercise of a trust power, the Jersey court could possibly come to your rescue and set aside the offending transaction.

How can the Jersey court help?

Under the Trusts (Jersey) Law 1984 (as amended) ("**Law**"), if it can be proven that the person bringing the application before the court:

1. **made a mistake**, in relation to a transfer or other disposition of property to a trust, or in relation to the exercise of his or her power;
2. **but for that mistake**, they would not have made such a transfer or other disposition, or would not have exercised the power or would not have exercised the power in the way it was exercised; and
3. **the mistake is of so serious a character**;

the Jersey court has power to declare that the transfer, or exercise of a power, be set aside. The consequence of that declaration is that any tax liability which resulted from such a transfer or exercise of a power, subsequently falls away.

Is this sounding too good to be true? Well, it's not! Keep reading...

Mistake Applications

Article 47 of the Law provides a statutory basis for relief to be granted for reasons of mistake. In particular, **Article 47E** deals with the Court's power to set aside a transfer or disposition of property made to a trust due to a mistake following an application by the settlor, his or her personal representatives, or successors in title. **Article 47G** deals with the Court's power to set aside the exercise of powers in relation to a trust or trust property due to a mistake following applications from the trustee (or the person exercising the power), a beneficiary, an enforcer, the Attorney General (for charitable trusts), or any other person with the leave of the Court.

In order to render it just for the Court to make a declaration of mistake under either Article, the person bringing the application must satisfy the three limb test (as set out above).

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Recent Cases Before the Jersey Court

Throughout this summer, in particular, the Royal Court has heard and handed down several decisions in relation to the exercise of its powers under these Articles. To give you a flavour of the types of mistakes that have been made, we have summarised three recent cases.

In the matter of the G Trust

This case concerned an application under Article 11 and Article 47E of the Law, to declare a trust invalid on the grounds of mistake as to tax consequences. The Settlor in the matter held cash assets in Luxembourg, which upon positive advice, he transferred into a UK bank account. Sums were then settled out of the UK bank account, together with a portfolio of investments (some of which comprised UK situs assets), into a Jersey trust.

The transfer of the UK situs assets, gave rise to a 20% inheritance tax liability. Due to the seriousness of the tax consequences, which were prejudicial to the trust, and on the basis that but for the mistake the tax liability would not have occurred, an application was made to the Court to set the trust aside. The Court granted the orders sought with the effect being that the trust was voided, as if it had never existed.

In the matter of the E Settlement

This case concerned an application under Article 47G and/or Article 47H (power of the Court to set aside the exercise of fiduciary powers in relation to a trust or trust property) of the Law, to avoid the trustee's decision to demand and subsequently receive a payment of interest due on a loan in the sum of £2,285,111.83. As the company that paid the interest was a UK company, the interest paid was considered a UK source of income, and as such, the trust became liable to pay tax at a rate of 45%.

The income tax liability in this particular instance amounted to just over £1 million. Had the trustee known about the tax liability, they would not have made the demand for the interest or they would have dealt with it in another, more efficient, manner. Confirming previous authorities, and considering the detriment to the trust being sufficiently serious, the Court granted relief to the trustees under both Articles 47G and 47H.

A & B v C

This is another case which concerned an application under Article 47G and/or 47H of the law, to set aside a disposition from one trust ("the Old Trust") to another ("the New Trust"). The New Trust was established in order to access an unrealised stockpile of gains in the Old Trust. A scheme was devised whereby the capital that was received into the New Trust would be ostensibly unrelated to the unrealised gains from the Old Trust, thus avoiding capital gains tax. Full tax advice was given prior to the transfers into the New Trust, with no risks being identified.

Many years later it became apparent, through conflicting legal advice, that the New Trust would be liable to UK Inheritance Tax and the Settlor would be subject to capital gains tax. Once again the Court considered the tax liabilities to be sufficiently serious and set aside the transfers to the New Trust and reinstated the Old Trust, which had been subsequently terminated. It was said that no reasonable

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trustee would have taken the steps which led to the transfers into the New Trust, had they known the outcome of this would be an exposure to significant tax liabilities. The Court indicated that, in deciding applications involving Articles 47E – 47H of the Law, it will take a holistic approach with a view of achieving an equitable solution to the issues before the Court.

Interestingly, in the latter cases, despite HMRC being advised of the applications, no request to intervene was received. Whether HMRC will continue to take this approach is unclear, but for now its comforting to know.

Types of Mistakes

If you are in any doubt as to what types of mistakes have been made in previous cases and whether your mistake may also benefit from the assistance of the Jersey court, for ease, we list some of the most common scenarios that have given rise to actionable mistakes below:

1. a settlor not having taken any tax advice prior to establishing a trust;
2. a trustee not having insisted on receiving a copy of the tax advice that they believed to have been obtained prior to the establishment of a trust;
3. a leading law firm having provided incorrect advice;
4. a leading accountancy firm having provided incorrect tax advice; and
5. a settlor not having understood the terms of the trust.

This remedy does not only apply to trusts that are governed by Jersey law. The Jersey court has previously applied the remedy of mistake to an English trust that was administered by a Jersey based trustee.

If you would like to speak with someone about a potential mistake application, please do not hesitate to contact us. An update on the Guernsey position will follow shortly.

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