GL v Nautilus Trustees Ltd

Jurisdiction:	Jersey
Judge:	The Deputy Bailiff
Judgment Date:	14 August 2009
Neutral Citation:	[2009] JRC 164A
Reported In:	[2009] JRC 164A
Court:	Royal Court
Date:	14 August 2009

Text

[2009] JRC 164A

ROYAL COURT

(Samedi Division)

Before:

M. C. St. J. Birt, **Esq**., Bailiff, **and** Jurats King **and** Liddiard.

In the Matter of The R Remuneration Trust

Between
GL
Representor
and
Nautilus Trustees Limited
Respondent

Advocate N. F. Journeaux **for the Representor**

Advocate L. K. A. Richardson **for the Respondent**

Authorities

Income and Corporation Taxes Act 1988.

Re E Trust [2008] JRC 053.

Gibbon v Mitchell [1990] 1 WLR 1304.

Sieff v Fox [2005] 1 WLR 3811.

Re DSL Remuneration Trust [2007] JRC 251.

Re A Trust Company Limited [2007] JRC 184.

The Deputy Bailiff

1 This is an application by the Representor to set aside a trust and certain gifts to that trust on the grounds of mistake. The Court granted the application at the conclusion of the hearing and now gives its reasons.

The Background

2 The Representor is a sole trader carrying on a successful business in the United Kingdom which employs over 200 people. He is married with three children.

3 In 1999, following an introduction from his accountants BDO Stoy Hayward, the firm of Baxendale Walker, English solicitors, advised him that he should set up what is known as a remuneration trust. He was advised by Baxendale Walker that the trust would allow him to:-

(i) reduce his tax liability as he could contribute pre-tax profits from his business to the trust;

(ii) set aside money to invest in his business as and when required by way of loans back from the trust;

(iii) provide benefits to his staff in a manner that reduced the tax liability of the business on those benefits, and;

(iv) allow the funds of the trust to be distributed to his family following his death.

4 Acting upon this advice he executed a trust deed (“the Trust”) on 15th March, 2000, with an

original fund of £100. He subsequently made additional transfers to the Trust of £2,250,000 on 28th March, 2000, US$750,000 in early 2001 and £1m on 11th May, 2001, ("the transfers"). The trust deed was entered into between the Representor (described as "the Founder") and Atlas Trust Company Limited (Jersey) Limited ("Atlas") as original trustee.

5 The Trust was a discretionary trust and the beneficiaries were defined as the present, past and future employees from time to time of the Founder and the wives, husbands, widows, widowers, children, step-children and remoter issue of such employees and the spouses and former spouses of such children and remoter issue. There was a further provision that no Excluded Person could be a beneficiary. By schedule 2 of the trust deed, Excluded Person was defined to include the Founder and any person 'connected with' the Founder, where 'connected with' had the meaning ascribed to the expression by the Income and Corporation Taxes Act 1988 (" ICTA".)

6 The trust deed conferred a power of amendment upon the Representor as Founder to be exercised with the consent in writing of the trustee, but this power was restricted so that it could not be used to alter the provisions of Clause 10 or any of the provisions concerning Excluded Persons.

7 The relevant provisions of Clause 10 are as follows:-

> " ***10.1 Notwithstanding anything to the contrary expressed or implied in this Deed, no power or discretion hereby or by law conferred on the Trustees shall be exercisable nor exercised by the Trustees in such manner as to cause any part of the Trust Fund or the income thereof…..*** to become payable to or applicable for the benefit of the Founder…
>
> ***10.2 Notwithstanding anything to the contrary express or implied in this Deed, no dispositive duty or power hereby or by law conferred on the Trustees shall be exercisable nor exercised by the Trustees so as to cause Trust Funds to be distributed to or for the benefit of any Beneficiary UNLESS, had the Founder been the legal and beneficial owner of such property, such a hypothetical expenditure by the Founder would have constituted an expense incurred wholly and exclusively for the purposes of the Trade and for no other purpose."***

8 Para 1.2.16 of the First Schedule to the trust deed conferred a power on the trustees to lend any part of the trust fund to any person and to provide guarantees to any person (including the Founder) whether or not taking security for the same and on such terms as the trustees may think fit. As well as a loan to the Representor in May 2000, which was subsequently repaid, the Trust has made the following loans to the Representor, (as Founder), namely £150,000 in June 2004, £25,000 in December 2005, £22,000 in December 2006, and finally £2.4m on 1st June, 2007, to finance the establishment of a production facility in Lithuania.

9 Between December 2000 and December 2004 the Trust made a series of discretionary bonus payments to various members of staff as incentives for those staff members to remain loyal to the business. These payments were invariably made at the instigation of the Representor with the names and amounts of bonuses suggested. In addition, the cost of some Christmas parties and hampers as gifts for the staff of the business were met by the Trust during this period.

10 On 30th November, 2005, the Representor exercised his power to amend the trust deed by deed of amendment which provided that:-

> " ***The class of beneficiaries of the trusts hereof shall not include, as from 1 November 2002, any employee or former employee of the Founder (but shall continue to include spouses, dependants and remoter descendents of such descriptions of person).***"

This deed was executed on advice from Baxendale Walker for reasons unconnected with the present application. The effect was that the only beneficiaries of the Trust as at the date hereof are the wives, husbands, widows, widowers, children, step children and remoter issue of present, past and future employees and the spouses and former spouses of such children of remoter issue plus future employees.

11 On 29th February, 2008, Nautilus Trustees Limited ("Nautilus") was appointed as trustee in place of Atlas.

12 The Representor has been advised that, contrary to his understanding at the time of the creation of the Trust:-

He contends that he would not have established the Trust had he known that this was the position. Accordingly, he now seeks to set aside the Trust and the transfers on the grounds of mistake.

Who should be convened?

> (i) The Trust cannot make loans to him in the manner envisaged at the time of the Trust's creation, and;
>
> (ii) his wife and children may not become beneficiaries of the Trust following his death.

13 The Representation was first presented before the Court on 26th June, 2009. On that occasion it was ordered that Nautilus, as trustee of the Trust, be convened. However, the Court does not appear to have been invited to consider whether any of the beneficiaries should be convened or whether someone (whether one of the beneficiaries or an advocate) should be appointed under RCR 4/4 to represent the interests of the beneficiaries.

14 When the matter came on for hearing, we invited submissions as to whether it would be right to proceed in the absence of a representative of the beneficiaries.

15 Mr Journeaux referred us to paragraph 21 of the judgment of the Court in *Re E Trust* [2008] JRC 053 where the Court said:-

> " ***When the Court sits in its supervisory capacity to consider directions or rulings it should give in relation to a trust, it has to consider in each case who should be convened at the hearing.*** The starting point is that the trust property is held beneficially for the beneficiaries and accordingly it is normally appropriate that they should be convened (see *Re A Settlement* [1994] JLR 139 at 144 ***per Bailhache, Bailiff).*** However, as that case made clear, it is not invariably the case that all the beneficiaries need to be heard. Many of them may have an identical interest; alternatively their interest may be extremely remote. It is ultimately a matter for the discretion of the Court as to which beneficiaries should be convened having regard to the nature of the particular application and the particular circumstances."

16 We also bear in mind the terms of RCR 4/5 which reads as follows:-

> " ***(1) Proceedings may be brought by or against trustees ….*** in their capacity as such without joining any of the persons having a beneficial interest in the trust ….; and any judgment or order given or made in those proceedings shall be binding on those persons unless the Court in the same or other proceedings otherwise orders on the ground that the trustees…. could not or did not in fact represent the interests of those persons in the first mentioned proceedings.
>
> ***(2) Paragraph (1) is without prejudice to the power of the court to order any person having such an interest as aforesaid to be made a party to the proceedings or to make an order under Rule 4/4."***

17 Mr Journeaux argued that, on the facts of this case, it was not necessary to convene any of the beneficiaries or appoint a representative because the trustee was well placed to put forward any possible arguments on their behalf. Furthermore, the interests of the beneficiaries were remote for the reasons referred to later. Miss Richardson, on behalf of the trustee, supported Mr Journeaux and confirmed that the trustee was conscious of its responsibility to look at the matter from the point of view of the beneficiaries. She pointed out that, in the leading case on mistake of *Gibbon v Mitchell* [1990] 1 WLR 1304, Millett J had not thought it necessary to join or hear from those who would lose out if the trust were set aside, namely the unborn children and remoter issue. We were referred in particular to Millett J's observation that such persons were all volunteers and could not conscionably insist upon their legal rights under the deed once they had become aware that it had been executed under a mistake. On the other hand, in *Sieff v Fox* [2005] 1 WLR 3811, *Re DSL Remuneration Trust* [2007] JRC 251 and *Re A Trust Company Limited* [2007] JRC 184, those with an interest in upholding the transaction alleged to be vitiated by mistake were

heard in opposition to the claim.

18 We were persuaded that, on the facts of this particular case, it was not necessary to convene the beneficiaries or some of them or to appoint a representative under Rule 4/4. We would summarise our reasons as follows:-

(i) We agree that, as explained later, the interest of the beneficiaries is remote.

(ii) We are satisfied that Nautilus as trustee has taken its obligation to look after the interests of the beneficiaries very seriously. It has instructed Miss Penelope Reed QC to advise on whether there are grounds to oppose the Representor's application to set aside the Trust and the transfers and we have seen that opinion. It is clear that Miss Reed has considered the position very thoroughly and indeed has raised a number of matters in connection with the Representor's application which have forced a rethink to some extent. Miss Reed has given us her opinion that she is not sure what would be gained by representatives of the beneficiaries being joined, bearing in mind that it is the duty of the trustees to put forward any possible arguments in opposition to the claim. Her advice is that she does not think that the claim can be resisted. Miss Richardson has confirmed that, had the trustee concluded that there was an arguable case against the claim, it would have put such arguments before the court.

19 However we wish to record that we do not think that the correct procedure was followed in this case. The representation was tabled on a Friday afternoon and the court was simply asked to convene the trustee. It was not specifically asked to consider whether any beneficiary should be convened or a representative appointed. The setting aside of a trust on grounds of mistake will normally be contrary to the interests of the beneficiaries. The starting point should therefore be that they should be given the opportunity of being heard in opposition to the claim. We accept that this is only a starting point and it may be that the court is satisfied that they do not need to be convened or represented. However, the person bringing the application must specifically make the court aware that he is seeking not to convene any of the beneficiaries and he must invite the court to rule on whether it agrees with him. It may be that, as Mr Journeaux submitted, there is insufficient time to consider such a matter on a Friday afternoon; but in that event the matter can usually be adjourned to 9.30am one day the following week for a very short procedural hearing before the presiding judge alone. In essence, the question of whether to convene any beneficiaries or appoint a representative should actively be brought to the court's attention at an early stage so that a decision can be taken then rather than the point being raised by the court at the last moment as occurred in this case, with the consequent risk of an adjournment and extra expense and inconvenience to the parties.

The law on mistake

20 The Trust is expressed to be governed by English law. The court has received opinions from Mr Daniel Hochberg of Willberforce Chambers on behalf of the Representor and from Miss Penelope Reed QC of 5 Stone Buildings on behalf of the trustee.

21 Whilst there are certain differences between counsel as to the application of the law to the facts of this particular case, there is complete agreement between them as to the law itself. This is to be found in the decision of Millett J in *Gibbon v Mitchell* [1990] 1 WLR 1304 where he said at 1309:-

> " ***In my judgement, these cases show that, wherever there is a voluntary transaction by which one party intends to confer bounty on another, the deed will be set aside if the court is satisfied that the disponor did not intend the transaction to have the effect which it did.*** It will be set aside for mistake whether the mistake is a mistake of law or of fact, so long as the mistake is as to the effect of the transaction itself and not merely as to its consequences or the advantages to be gained by entering into it…"

Both counsel refer to the fact that other cases have raised an issue as to whether the test is in somewhat wider terms than was laid down by Millett J (see for example the observations of Lloyd LJ in *Sieff v Fox* [2005] 1 WLR 3811) but they are agreed that any mistake in this case was as to the effect of the disposition and therefore falls within the narrower test laid down by Millett J.

The mistakes

(i) Loans

22 The Court has received affidavits from the Representor and Miss Jehan on behalf of Nautilus. The Representor has exhibited to his first affidavit copies of a number of documents which were supplied by Baxendale Walker to him before he established the Trust. We are quite satisfied from the evidence that the Representor understood that he would be able to borrow money from the Trust in order to invest in his business when he required it. He understood that these loans would bear interest at a commercial rate but that they would be what Baxendale Walker called "deeply discounted", which meant that no payments of interest or repayments of capital would be required during the currency of the loans but only when the term of the loan expired. He was also told that the loans could be rolled over and continue to remain outstanding until the time of his death, and that, after his death, the loans would be repaid to the Trust from his free estate together with the rolled up interest. He was told that this would reduce his free estate for inheritance tax purposes. He further understood that security for such loans would not be required.

23 As we have indicated earlier, various loans were made by the Trust to the Representor on this basis. However, following another case concerning a similar trust, Atlas reviewed the legal position and concluded that it could not properly make loans in the manner envisaged. Accordingly it refused an application by the Representor for a further loan in December 2007. The Representor has made it clear, and we accept that, had he known that he could not receive loans on the basis described above, he would not have established the Trust.

24 Mr Hochberg and Miss Reed have reviewed the trust deed and concluded that the trustee is quite justified in concluding that it cannot properly make loans on the terms described above. Although para 1.2.16 of Schedule 1 of the trust deed enables the trustees to make loans to any person including the Founder, this is subject to clause 10.1 (quoted at para 7 above) which provides that no power or discretion may be exercised so as to cause any part of the trust fund to be applied for the benefit of the Founder. Unless loans on the terms envisaged could be obtained from a commercial lender, they would constitute a benefit arising to the Representor under the Trust and accordingly are not permitted. It is accepted that loans on such terms would not be available from a commercial lender.

25 In the circumstances, both counsel are agreed that the Representor was acting under a mistake of fact, namely that the trustee had power under the terms of the Trust to make loans to him on terms more favourable than commercial terms, as regards rolling up of interest, no need to provide security, and ability to extend the terms of the loans indefinitely. Furthermore they are agreed that this is a mistake as to the effect of the transaction falling within the narrower test of *Gibbon v Mitchell* and that accordingly the equitable jurisdiction to set aside the Trust and the transfers to the Trust for mistake is engaged.

(ii) Whether the family can be beneficiaries after the Representor's death

26 The Representor also relies upon a second mistake. The evidence shows that the Representor was advised that, following his death, his wife and children could become beneficiaries of the Trust so that the assets of the Trust could be applied for their benefit. We accept that this aspect was crucial to the Representor and that he would not have created the Trust or made the transfers had he not believed this to be the case.

27 However, a question has arisen as to whether this is in fact a mistake. The argument goes as follows: The Representor's wife and children are undoubtedly Excluded Persons at present because they are ‘connected with’ the Representator (as Founder) under S839 ICTA. The trustee was originally advised that this ‘connection’ continued after death with the consequence that the wife and children could not be added as beneficiaries at that stage because they would remain Excluded Persons. However, Miss Reed has advised that it is strongly arguable that persons are only connected under S839 when both are alive. Accordingly, once the Representor is dead, the wife and children will no longer be Excluded Persons as they will no longer be ‘connected with’ the Representor. She accepts that there is an issue as to how they can be added as beneficiaries. The Representor has power to amend the Trust under Clause 9 but he cannot do so in favour of Excluded Persons. Once he is dead and they are no longer Excluded Persons, he will not be in a position to amend the trust deed. The only answer that she can think of is if, during his life, the Founder can amend the Trust under Clause 9 prospectively to include his wife and children as beneficiaries after his death.

28 Having seen Miss Reed's opinion, Mr Hochberg has carried out further research. Although there is no direct authority, he accepts that, for the reasons set out in his supplementary opinion, it is certainly arguable that connected persons ceased to be connected for the

purposes of S839 on the death of one of them. However, he is also of the view that it is not clear whether the Representor could validly exercise his power of amendment under Clause 9 at this stage with prospective effect so as to constitute the members of his family as beneficiaries after his death. This is because, he advises, fiduciary powers can only be exercised in the light of the circumstances prevailing at the time of their execution, and not prospectively, since the circumstances at such future time may have changed significantly.

29 One is left therefore with the position that both counsel are uncertain whether a deed of variation under Clause 9 can validly be executed by the Representor during his life so as to add his wife and children as beneficiaries with effect from the date of his death. The question then arises as to whether such uncertainty amounts to a mistake as to the effect of the transaction so as to engage the court's equitable jurisdiction to set aside the transaction. The Representor has sworn a supplementary affidavit stating that the funds settled on the Trust represented a substantial proportion of his overall wealth and of his ability to provide for his wife and children after his death. He states that if he had been advised that there was any uncertainty as to whether his wife and children could benefit from the Trust after his death, he would not have created it and transferred funds to it. Mr Hochberg gives as his opinion that the Representor can rely on his mistake in believing that the wife and children could with complete certainty benefit under the Trust as a ground for setting it aside. However, he does not refer to any authority in support of that opinion. Miss Reed does not consider this aspect in her opinion and has not been asked to advise upon it.

30 On the current state of the evidence we would prefer not to reach a concluded view on whether the second mistake relied upon is made out. One starts from the proposition that, before it can grant relief, the Court must be satisfied on the balance of probabilities that a mistake as to the effect of the transaction has been made. The question arises as to when a mistake has been made. On the one hand, one can understand the argument of Mr Hochberg that, if a settlor proceeds on the basis that a trust deed definitely achieves a particular effect, a discovery that in fact the position is uncertain and it is not clear whether the deed achieves the desired effect, can be said to amount to a mistake as to the effect of the deed. On the other hand, if the uncertainty is capable of easy resolution by obtaining a decision from the Court as to the correct interpretation of the deed, can it be said that there is a mistake as to the effect of the deed unless or until the court has ruled as a matter of interpretation that the deed does not have the intended effect? Thus, in this case, should the court, before finding that there has been a mistake, insist that the Representor exercise his power of amendment prospectively to add his family as beneficiaries after his death, with the matter then being referred to the court for a ruling on the validity of the amendment? If the court were to hold the amendment to be valid, there would not in fact have been a mistake as to the effect of the trust deed. Conversely, if the court ruled against the exercise of the power of amendment, there would clearly have been a mistake. Should the court require parties to take such steps – which may be quite expensive – or is it sufficient that the position is uncertain and therefore arguably the deed has not achieved the intended effect?

31 We express no view as to these competing arguments, not least because they have not been fully explored in the opinions of English counsel and this is a trust governed by English law. Furthermore, it is not necessary to do so. As already indicated, we are satisfied that the Representor was acting under a mistake as to the effect of the Trust in relation to the ability to make loans on the terms envisaged and that he would not have created the Trust or made the transfers had he not been acting under such a mistake. We are content to proceed on the basis of that mistake alone.

Discretion

32 The Court has a discretion as to whether to set aside a transaction entered into under a mistake. Two factors which the Court will take into account in deciding whether to exercise the discretion to set aside a settlement on the grounds of the mistake of the settlor as to its legal effect are, first, whether it would be unjust on the beneficiaries for the settlement to be set aside, and second, whether the position of third parties would be prejudiced if the settlement were to be set aside.

33 In relation to the beneficiaries, they now fall into two groups following the execution of the deed of 30th November, 2005, which excluded present and past employees. The first group consists of future employees and the second group consists of the specified relatives and dependents of past, present and future employees. The evidence shows that, prior to the execution of the deed of 30th November, 2005, the Trust made a series of discretionary bonus payments to various members of staff as incentives for those staff members to remain loyal to the business. Those payments were made at the instigation of the Representor by sending a letter to the trustee with the names and suggested amounts of the bonuses. In addition, the costs of some Christmas parties and hampers as gifts for the staff were met by the Trust. Although the Representor thought the total amount of these payments did not exceed £175,000, the evidence from Miss Jehan suggests that the total was some £117,000. The payments made to staff were purely discretionary and did not fall within their contractual remuneration. Since the execution of the deed of 30th November there has been no ability to make discretionary bonus payments to current employees. The Representor has continued to make payments of staff bonuses and other benefits similar to that previously made from the Trust, but has done so directly from his business.

34 We are satisfied that it is highly unlikely that the current beneficiaries will benefit to any substantial degree from the Trust. As to future employees, they are only beneficiaries between the moment of their identification as a future employee and the commencement of their employment (at which time they cease to be beneficiaries). Thus, the only realistic benefit which might be paid to them would be some form of golden hello. As to the second group of beneficiaries, the trustee would have to bear in mind the provisions of Clause 10.2 which only permit distributions for the benefit of the beneficiary if, had there been payment made by the Representor (as Founder), such expenditure would have constituted an expense incurred wholly and inclusively for the purposes of the Founder's trade. This clearly imposes a substantial restriction on the ability of the Trust to make payments to relatives and dependants of employees.

35 Furthermore the Court must bear in mind the observations of Millett J in *Gibbon v Mitchell* [1990] 1 WLR 1304 where he said this at 1310:-

> " ***Equity acts on the conscience.*** The parties whose interest it would be to oppose the setting aside of the deed are the unborn future children of Mr Gibbon and the objects of discretionary trust to arise on forfeiture, that is to say his grandchildren, nephews and nieces. They are all volunteers. In my judgment they could not conscionably insist upon their legal rights under the deed once they had become aware of the circumstances in which they had acquired them."

36 The Representor has confirmed that if the Trust is set aside, and subject to the ability of the business to afford to do so, it is his current intention that, in the future, he would give the same consideration to making payments of bonuses to selected staff, and provision for social events and the like for current employees of the business as he had asked the trustees to consider making prior to the execution of the deed excluding current employees. Given the important consideration referred to by Millett J above and the unlikelihood of the current beneficiaries benefiting from the Trust, the court is quite satisfied that it would not be unjust on the beneficiaries for the Trust and the transfers to be set aside.

37 As to the position of third parties, if the deed is set aside, the Representor will have a theoretical claim against the trustee for the £117,000 distributed to beneficiaries and the trustee in turn may have a claim against those beneficiaries, although any such claims would be subject to a defence of change of position. However, the Representor has confirmed that he will not seek restitution of these amounts and that Altas and Nautilus may retain trustee fees and disbursements which have been charged. Both of these aspects will be recorded in the order of the court. The loan position does not cause any difficulties. Although the Representor is indebted to the trustee, he will owe money to himself once the Trust is set aside and accordingly no difficulty arises.

38 In all the circumstances we are satisfied that there is no good reason for the court not to exercise its discretion to set aside these transactions on the grounds of the Representor's mistake. Accordingly we make an order setting aside the Trust and the transfers.