First Names (Jersey) Ltd v Advocate Jeremy Heywood (as representative of the adult beneficiary)

Jurisdiction:	Jersey
Judge:	Sir Michael Birt, Jurats Olsen, Sparrow
Judgment Date:	10 August 2018
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Text

[2018] JRC 143

ROYAL COURT

(Samedi)

Before:

Sir Michael Birt, **Commissioner, and** Jurats Olsen **and** Sparrow

In the Matter of the E Settlement

Between
First Names (Jersey) Limited
Representor
and
Advocate Jeremy Heywood (as representative of the adult beneficiary)
First Respondent

and

Advocate Jeremy Heywood (as guardian ad-litem of the minor beneficiary)
Second Respondent

Advocate N. M. Saunders **for the Representor**.

Advocate J. N. Heywood **in person**.

Authorities

Trusts (Jersey) Law 1984.

Pitt v Holt [2013] UKSC 26.

Royal Court Rules 2004.

Re Onorati Settlement [2013] (2) JLR 324.

Trust — reasons for the court granting the relief sought.

THE COMMISSIONER:

1 This is an application by the Representor ("the Trustee") as trustee of a settlement ("the Trust") for an order under Article 47G and/or Article 47H of the Trusts (Jersey) Law 1984 ("the Law") avoiding its decision to demand (and subsequently receive) payment of interest due under certain loan notes.

2 At the conclusion of the hearing, the Court announced its decision to grant the relief sought and said that it would give reasons later. What follows constitutes those reasons.

The factual background

3 The settlor of the Trust ("the settlor") is a woman of some means who created the Trust by deed dated 24 th October, 1988. It is a discretionary trust in conventional form governed by the law of Jersey. The beneficiaries consisted originally of the children and remoter issue of the settlor. However, in 2006, the predecessor trustee of the Trustee executed a revocable deed of exclusion which excluded the settlor's two daughters and their issue as beneficiaries. The result is that since then the class of beneficiaries has consisted of the only son of the settlor ("the son"), who is an adult, and the only child of the son ("the grandson") who is a minor.

4 In 2013, one of the assets of the Trust consisted of a company incorporated in the British Virgin Islands ("the Company") which in turn owned a property in London. The settlor wished to acquire that property which was situated adjacent to another property which she indirectly owned. By an agreement dated 20 th May, 2013, the Trustee, as trustee of the Trust, agreed to sell the shares in the Company to an English company ("the Purchaser") which was indirectly owned by the settlor. The sale price was £18,251,970 of which £251,970 was payable upon completion, the balance of £18m being payable on or before 31 st December, 2013. The sum of £251,970 was duly paid upon completion of the sale.

5 The settlor apparently felt that the sum of £18m could be more profitably used elsewhere and suggested that payment of the deferred consideration be further deferred. This was agreed to by the Trustee subject to accrual of interest at 5% compounded semi-annually until payment. Thus, on 31 st December, 2013, the Trustee subscribed for £18m of 5% fixed rate unsecured subordinated loan notes ("the Loan Notes") issued pursuant to a loan note instrument of that date issued by the parent company of the Purchaser ("the Parent Company"), in exchange for which the Trustee released the Purchaser from any obligation to pay the deferred consideration. The Parent Company is a company incorporated in England and Wales and the Loan Notes were quoted Eurobonds.

6 The terms of the Loan Notes provided for interest on the sum of £18m to accrue and to be compounded semi-annually, but conferred an ability upon the Trustee to demand payment of interest. In June 2016, the Trustee had need of income. Its assets, though substantial, were essentially illiquid and it had been making payments towards the maintenance and education of the grandson and expected to continue doing so.

7 Accordingly, on 3 rd June, 2016, the Trustee made formal demand for payment of interest in the sum of £2,285,111.83 ("the Demand") and this sum was duly paid by the Parent Company to the Trustee.

8 The Trustee has subsequently been advised that this payment of interest has given rise to a liability to income tax in the UK. That is because the Parent Company is a UK company so that interest paid amounts to UK source income. Under the relevant tax provisions, a trust such as the Trust has to pay tax on UK source income at a rate of some 45%. The income tax liability of the Trust therefore amounts to just over £1m. The Trustee has been advised by Smith & Williamson ("S&W") that, had it established a non-UK resident company which was wholly owned by the Trust and assigned the Loan Notes to that company prior to the Demand, there would have been no income tax liability on the Trustee or on the assignee company upon payment of the interest.

Tax advice

9 At the time of the sale of the Company and the subsequent creation of the Loan Notes, the Trustee was advised on tax matters by S&W. Its English solicitors were the firm of Taylor

Wessing. KPMG was advising the Parent Company in connection with the Loan Notes and that firm emailed S&W on 19 th December 2013 to say that the Parent Company's preferred route was for the notes to be structured as quoted Eurobonds as this would remove the need for the Parent Company to deduct withholding tax on payments of interest.

10 On 29 th December, 2013, having reviewed the draft documentation, Mr Bursby of Taylor Wessing emailed Mr Rodgers of S&W (copied to the Trustee) raising one or two points on the documents but going on to say:-

> *"Lastly, we have not considered the tax consequences of the Trust agreeing to the loan notes in lieu of the deferred consideration nor in the time available have we reviewed the articles of [the Parent Company] nor taken legal advice on whether these Loan Notes can be listed on the Channel Islands Stock Exchange."*

11 The next day, Mr Rodgers emailed Taylor Wessing (copied to the Trustee) on the points made by Taylor Wessing and in relation to tax said simply this:-

> *"Smith & Williamson has advised on the tax treatment of the interest to the Trustee's satisfaction."*

12 Despite this comment, the evidence before the Court is that neither the Trustee nor S&W can find any note or record of any such advice in their files. Accordingly, it is not known to what Mr Rodgers was referring in that email.

13 On 6 th July, 2015, S&W presented their annual UK taxation review in connection with the Trust to the Trustee. Paragraph 1.1 describes the report as an outline of the UK taxes that may apply to the Trust. Paragraph 1.3 asserts that the Trustee would only be subject to UK tax on any UK source income and that the Trust has no UK source income for the period to 31 st December, 2014.

14 It appears that the accounts of the Trust for the period ending 31 st December, 2014, were supplied to S&W for the purposes of the 2015 review and that these accounts showed the details of the Loan Notes and the accrued interest thereon. The correspondence exhibited to the affidavit sworn on behalf of the Trustee by Mrs Claire Kelly, a senior manager, discloses a difference of opinion between the Trustee and S&W as to whether S&W should have alerted the Trustee to the fact that interest on the Loan Notes was UK source income and that actual payment (as opposed to accrual) of such interest would lead to a charge to UK income tax on the interest paid. S&W assert that the 2015 review was correct and that, because interest on the Loan Notes had only been accrued at that date, there was no UK source income and no UK tax liability. The Trustee, on the other hand, argues that it should have been alerted by S&W to the fact that actual payment of the interest would be UK source income and would lead to a charge to UK tax.

15 It is not for us to reach a view on this difference of opinion for the purposes of these proceedings. What is clear is that the Trustee did not realise in June 2016 that payment (as opposed to accrual) of interest would lead to a charge to UK income tax payable by the Trustee out of the trust fund. It took no tax advice at the time of the Demand and treated the demand for payment of accrued interest as a purely administrative matter. We also accept the assertion by Mrs Kelly that, had the Trustee been alerted to the correct tax position, it would have followed the course referred to earlier and assigned the Loan Notes to a wholly owned non-UK resident company (e.g. a Jersey company) of the Trust before claiming payment of any interest. This simple step would have resulted in no charge to UK income tax on the payment of interest on the Loan Notes.

The statutory provisions

16 Article 47G of the Law is, so far as relevant, in the following terms:-

> ***"47G. Power to set aside the exercise of powers in relation to a trust or trust property due to mistake*** .
>
> ***(2) The court may on the application of any person specified in Article 47I(2), and in the circumstances set out in paragraph (3), declare that the exercise of a power by a trustee or a person exercising a power over, or in relation to a trust, or trust property, is voidable and –***
>
> ***(a) has such effect as the court may determine; or***
>
> ***(b) is of no effect from the time of its exercise*** .
>
> ***(3) The circumstances are where the trustee or person exercising a power –***
>
> ***(a) made a mistake in relation to the exercise of his or her power; and***
>
> ***(b) would not have exercised the power, or would not have exercised the power in the way it was so exercised, but for that mistake, and***
>
> ***the mistake is of so serious a character as to render it just for the court to make a declaration under this Article."***

17 'Mistake' is defined by Article 47B(2) as follows:-

> ***(2) In Articles 47E and 47G, "mistake" includes (but is not limited to) –***
>
> ***(a) a mistake as to –***
>
> ***(i) the effect of*** ,
>
> ***(ii) any consequences of, or***

(iii) any of the advantages to be gained by ,

a transfer or other disposition of property to a trust, or the exercise of a power over or in relation to a trust or trust property;

(b) a mistake as to a fact existing either before or at the time of, a transfer or other disposition of property to a trust, or the exercise of a power over or in relation to a trust or trust property; or

(c) a mistake of law including a law of a foreign jurisdiction."

18 Article 47H of the Law puts into statutory form the Hastings-Bass principle as it was understood to be prior to the decision of the Supreme Court in *Pitt v Holt* [2013] UKSC 26. It is in the following terms:-

"47H Power to set aside the exercise of fiduciary powers in relation to a trust or trust property .

(2) The court may on the application of any person specified in Article 47I(2), and in the circumstances set out in paragraph (3), declare that the exercise of a power by a trustee or a person exercising a power over, or in relation to a trust, or trust property, is voidable and –

(a) has such effect as the court may determine; or

(b) is of no effect from the time of its exercise .

(3) The circumstances are where, in relation to the exercise of his or her power, the trustee or person exercising a power –

(a) failed to take into account any relevant considerations or took into account irrelevant considerations; and

(b) would not have exercised the power, or would not have exercised the power in the way it was so exercised, but for that failure to take into account relevant considerations, or that taking into account of irrelevant considerations .

(4) It does not matter whether or not the circumstances set out in paragraph (3) occurred as a result of any lack of care or other fault on the part of the trustee or person exercising a power, or on the part of any person giving advice in relation to the exercise of the power."

19 Article 47I(2) provides that any application under Article 47G(2) or 47H(2) may be made by the trustee who exercised the power concerned.

Discussion

20 When the representation was first presented on 16 th March, 2018, the Court ordered that Her Majesty's Revenue and Customs ("HMRC") be sent a copy of the representation and informed of its right to apply to intervene. That subsequently occurred but HMRC has not made any application to intervene. On the same occasion, the Court appointed Advocate Heywood as representative of the son pursuant to Rule 4/4(2)(b) of the Royal Court Rules 2004 and as guardian ad litem of the grandson.

21 We are satisfied that the requirements of Article 47G of the Law are satisfied as submitted by Advocate Sanders for the Trustee and by Advocate Heywood for the beneficiaries. Thus:-

(i) The Trustee made a mistake as to the consequences of its decision to demand payment of accrued interest on the Loan Notes. It believed that there would be no UK tax consequences as a result of its decision whereas in fact payment of accrued interest led to a charge to UK income tax at 45% on the interest paid.

(ii) The Trustee would not have exercised the power to demand payment of interest if it had not made that mistake. Although it needed to obtain some income for the maintenance and education of the grandson, there was an easy alternative way of arranging payment of the interest. It would have assigned the Loan Notes to a wholly owned non-UK company which would then have demanded payment of the interest. The interest received by that company could then be paid to the Trust and hence applied for the maintenance and education of the grandson without any charge to UK tax.

(iii) We consider that the mistake is indeed of so serious a character as to render it just for the Court to declare the decision to demand interest voidable and to avoid it from the time of its exercise. The Demand has led to a charge to UK income tax payable out of the trust fund of a sum in excess of £1m. Payment of the sum will therefore prejudice the beneficiaries. The alternative would be for action to be taken by one or more of the beneficiaries against the Trustee and/or S&W. This would not be clear cut in view of the exoneration provisions in relation to the Trustee contained in paragraph 3 of schedule C of the trust deed and of the difference of position as between the Trustee and S&W referred to at paras 9 – 15 above. In any event, the Court remains of the view expressed in *Re Onorati Settlement* [2013](2) JLR 324 where the Court said at paragraph 44:-

"More generally, we are not attracted by the proposition that beneficiaries should be left to a remedy of bringing litigation against trustees or professional advisors. The beneficiaries are usually not at fault and have already incurred loss by reason of unnecessary tax charges. To force them to incur further expense in what may be uncertain litigation when the law allows for the avoidance of a decision made in breach of the trustees' duties seems unnecessary, undesirable and unjust."

22 *Onorati* was of course concerned with the Hastings-Bass principle rather than the law of mistake and the reference to a breach of duty by the trustees is now subject to the provisions of Article 47H(4) (quoted above) which makes it clear that a breach of duty is not required. However, the sentiment expressed in the above passage from *Onorati* seems to us to be equally applicable to decisions made by a trustee due to a mistake and whether it is just for the Court to grant relief under Article 47G.

23 We conclude that the decision of the Trustee to make the Demand should also be set aside under Article 47H. The Trustee failed to take into account a relevant consideration, namely the fact that demanding payment of interest would give rise to a substantial tax charge. It would not have exercised the power in that way but for its failure to take that relevant consideration into account.

24 Accordingly, this is a case which falls within both Articles 47G and 47H. It is for these reasons that the Court avoided the Trustee's decision and declared that the Demand and the receipt of interest pursuant thereto was of no effect from the time of the making of the Demand and the said receipt respectively. It further declared that the interest received pursuant to the Demand had been held on bare trust by the Trustee for the Parent Company since its receipt and ordered the Trustee to repay the sum forthwith to the Parent Company.

25 At the request of the Trustee, the Court made no order as to the costs of the representation.