Jersey's Royal Court declares trustee's exercise of power void

Insights - 10/01/2020

> **A mistake or a failure to take into account relevant considerations? The Royal Court is asked to consider its jurisdiction to declare voidable the exercise of a power on both grounds.**

On 3rd December 2019, the Royal Court declared void certain actions of a trustee (the "**Trustee**") by which the assets of two Jersey law trusts (together the "**Trusts**") were transferred into a circular ownerless corporate structure, terminating the Trusts.

Background facts

Certain beneficiaries of the Trusts were French tax residents. During the latter part of 2011, the Trustee was advised by Mr John Dewhurst of Chown Dewhurst LLP to transfer the assets of the Trusts to companies incorporated in the BVI in response to the introduction in France of tax legislation which was due to come into effect on 1 January 2012, namely the *Loi de Finances Rectificative* (the "**French Tax Legislation**"). Mr Dewhurst considered that the French Tax Legislation could lead to a change in the way in which foreign trusts are fiscally treated in France. As a result, he sought to engage the services of a French tax specialist, Maître Jean-Marc Tirard.

Mr Dewhurst proposed to the Trustee the form of corporate structure which was ultimately used, namely two BVI companies which would own each other. The Trustee then implemented the restructuring, under which:-

(a) The assets of the Trusts were transferred into newly incorporated holding companies, at that stage owned by the Trustee in its capacity as trustee respectively of each trust

(b) Two BVI companies were formed which owned each other ("**the BVI Structure**")

(c) The shares in the holding companies were transferred by the Trustee to one of the companies in the BVI Structure

(d) The Trustee entered into deeds by which the trust periods of the Trusts were brought forward to expire on the same day, thus bringing the Trusts to an end

(e) Consultancy agreements were entered into with two of the beneficiaries of the Trusts (which was the only way to extract value)

Thus, all trust assets were transferred out of the Trusts into a circular ownerless corporate structure ("**the 2011 Restructuring**").

Following the implementation of the 2011 Restructuring, the Trustee did not consider the French Tax Legislation applied to the assets held within the BVI Structure, as it no longer considered that the Trusts were in existence. It therefore never filed declarations with the French tax authorities.

French tax consequences

The Trustee first became aware of the potential implications of the 2011 Re-structuring in 2017. In early 2019, it obtained expert advice from a French tax lawyer who advised that:-

(a) The Trustee had in 2011 and still had reporting obligations to the French tax authorities

(b) The 2011 Restructuring would be viewed from a French tax viewpoint as having created a *de facto* or constructive new trust

(c) As the 2011 Restructuring has been implemented by the Trustee, it would be deemed to be the trustee of the new trust

(d) The Trustee should have filed an "Event Disclosure" with the French tax authorities before 31 December 2012 and disclosures each year from 2012

(e) The settlors of the Trusts may be taxed on the assets originally transferred into the Trusts

(f) The inheritance tax on the death of the settlors would be higher than if no “new trust” had been created (and the rate of inheritance tax is 60%)

(g) The French tax authorities were likely to regard the 2011 Restructuring as an artificial arrangement and might claim penalties up to 80% for "*fraudulent manoeuvres*"

The French tax advice was that if the transfer into the BVI Structure was set aside it would likely be viewed by the French tax authorities more favourably than the BVI Structure.

Mr Dewhurst accepted with the benefit of hindsight and on reviewing the files for the purposes of the application, that Maître Tirard did not provide specific advice on the BVI Structure nor did he

formally advise on the 2011 Restructuring, rather he only provided a general commentary in respect of certain aspects or relevant provisions of French law as they were understood at the time.

BVI law issues

In 2019, the Trustee also received BVI law advice in relation to the BVI Structure to the effect that:-

(a) The structure raised an issue of public policy, because it tied up property indefinitely without any clear legitimate public purpose or private benefit and it would not be clear what duties the directors of the two BVI companies would have in these circumstances

(b) If valid, it would seem that no one may benefit from the assets owned by the companies while the companies are in existence and after the dissolution of the companies its assets would either pass to the Crown or in trust to the Trustee, in its capacity as the trustee of the trusts from which those assets were appointed

Art 47G and 47H of the Law

The Trustee originally sought relief under Arts 47G or 47H of the Law. Art 47G permits the donee of a power to apply for a declaration that the exercise of that power in relation to a trust is voidable on the grounds of mistake. The guardian *ad litem* for the minor beneficiaries (and representative of the unborn class) argued that the application was best dealt with under Art 47H which similarly permits such a donee to seek relief where it has failed to take into account any relevant considerations or has taken into account irrelevant considerations.

The Court's decision and a trustee's duty to account

The Court agreed with the guardian *ad litem* and found as follows:-

(a) The only relevant tax advice was French tax advice and Mr Dewhurst confirmed that Maître Tirard did not formally advise on the 2011 Restructuring and the use of the BVI Structure. The Trustee therefore proceeded without considering the French tax implications of the 2011 Re-structuring.

(b) The Trustee proceeded without considering BVI law advice on the use of the BVI Structure or of Jersey law advice on the use of the relevant powers under the trust deeds to place the trust assets into such a structure. Without that advice, it was not possible for the interests of the beneficiaries to be considered.

The Court noted that it has in the past made clear that what may fall within the class of "*aggressive tax avoidance schemes*" may go to the exercise of its discretion to grant relief. The Court found that, however the 2011 Restructuring may be characterised, the most egregious aspect

of it was the transferring away of substantial assets to a circular ownerless set of entities, out of which no distributions could be made to the beneficiaries, with the possibility of all of it being lost to the Crown.

The duty of a trustee to account to the beneficiaries is at the core of the trustee/beneficiary relationship (Armitage v Nurse [1998] CH 241 at 253). The Court found that the beneficiaries in this case went from trusts where they were able to monitor their interests and hold the Trustee to account, to a corporate structure in which they appeared to have no such ability. The BVI advice made clear that there was a serious question over whether the directors of the BVI companies (provided by the Trustee) had any duties to perform for the former beneficiaries of the Trusts. Ordinarily directors owe their fiduciary duties to the shareholders as a whole, but in this case the directors of the BVI companies owed their duties to a company which was owned by the company of which they were directors.

The Court also noted that the beneficiaries under the Trusts had the added protection of the supervisory jurisdiction of the Court, but that the Court has no supervisory jurisdiction over companies (and certainly not BVI incorporated companies). The assets had been transferred to a BVI Structure which was on the face of it unaccountable.

There was no evidence that any of the beneficiaries (other than one) knew about the 2011 Restructuring and the Court could not see how any beneficiary, properly informed, would consider a transfer to an unaccountable circular ownerless structure from which no distributions could be made, to be in their interests, whatever the tax advice.

Accordingly, because the Trustee had failed to take very relevant considerations into account (French tax advice and BVI law advice) and had the Trustee taken those considerations into account it would not have exercised the relevant powers, the Court declared the transfers and the deed shortening the trust periods void.

In making those declarations, the Court concluded that notwithstanding the terms of Art 47H(4) (which allows the Court to set aside the exercise of a power irrespective of whether there was a lack or care or fault on the part of the person exercising the power), it was difficult to escape the conclusion that there was a lack of care on the part of the Trustee.

This case highlights the importance that trustees obtain detailed legal and tax advice when considering a restructuring of assets held in trust and is a helpful reminder that a trustee's duty to account is at the heart of the trustee/beneficiary relationship.

Advocate Damian Evans of Ogier was appointed guardian *ad litem* in this case.

About Ogier

Ogier is a professional services firm with the knowledge and expertise to handle the most

demanding and complex transactions and provide expert, efficient and cost-effective services to all our clients. We regularly win awards for the quality of our client service, our work and our people.

Disclaimer

This client briefing has been prepared for clients and professional associates of Ogier. The information and expressions of opinion which it contains are not intended to be a comprehensive study or to provide legal advice and should not be treated as a substitute for specific advice concerning individual situations.

Regulatory information can be found under Legal Notice

Meet the Author

Damian Evans

Partner

Jersey

E: damian.evans@ogier.com

T: +44 1534 514378

Key Contacts

Matthew Davies

Senior Associate

Jersey

E: matthew.davies@ogier.com

T: +44 1534 514132

Related Services

Dispute Resolution

Legal

Related Sectors

Trusts Advisory Group