We all make mistakes - but will the Jersey Royal Court have sympathy?

Insights - 19/10/2022

The law of mistake in Jersey is well established. The authorities make it clear that the Court will consider an application to set aside a trust and/or transfers onto trust on the grounds of mistake against three questions:

1. Was there a mistake on the part of the settlor in relation to the establishment of the trust or the transfers of assets into trust?
2. Would the trust or transfers into trust not have been made but for the mistake?
3. Was the mistake of so serious a character as to render it just for the Court to make a declaration?

The authorities also make it clear that the Court will generally look at the arrangements in respect of the trust in the round. And while every case will turn on its own facts, in many if not most cases, as has been observed by the Royal Court on numerous occasions, the transfer of property onto trust may occur at much the same time as the creation of the trust and the same mistake (assuming of course that the Court accepts there was a mistake) will be operating on the mind of the settlor both in relation to the creation of the trust and the transfer of property.

In Jersey, when considering such applications, the Royal Court does not make the distinctions made in English law (in particular by the Supreme Court in *Pitt v Holt* 2013 UKSC 26) as to mere causative ignorance or incorrect tacit assumption because in the Royal Court's view such distinctions would be artificial and therefore inappropriate.

Mere causative ignorance, it has said, is not one which reflects generally why such applications come before the Court. Ignorance is not usually the cause for the transfer to be made. The cause of the transfer is usually an intention to benefit the trust and the Court has observed that that is invariably not removed by the ignorance which might accompany it. More to the point, the Court has observed, is that a transfer would have been done in a different way had the transferor known what the effects or consequences of it might have been. And the intellectual space between mere

causative ignorance and incorrect tacit assumptions, the Court has said, is almost impossible to find because tacit assumptions will invariably be mistakes only when the person making the assumption is ignorant of some material fact.

In the recent judgment of the Royal Court *In the Matter of the E Settlement* [2022] JRC052 (the **E Settlement**), the Court has again confirmed that a settlor who is genuinely mistaken about the consequences of establishing a trust and/or transferring assets into trust will be looked upon with sympathy by the Court and relieved from having to engage in alternative risky litigation alleging negligence against professional advisers (with all the difficulties that may be incurred either with prescription, liability or remoteness of damage). It has emphasised that there is "all the difference in the world" between a settlor taking a calculated risk in making particular arrangements and a settlor who is genuinely mistaken about the risks which he is undertaking. There will be no sympathy for the former. The doctrine of mistake is not there to come to the aid of those who gamble and lose. The Court will have very little sympathy in that scenario.

If the Court is to be persuaded however that there has been a genuine mistake, it needs to be provided with all relevant correspondence and documents (including any privileged material) so that such an assessment can be made. A party seeking relief on the grounds of mistake will be expected to have interrogated any advice received in relation to the transfer they are seeking to set aside, the implication being they fail to do this, then the Court may have little sympathy and look unfavourably on an application to set the trust and/or any transfer aside.

The recent case before the English High Court of *Dukeries Healthcare Ltd v Bay Trust International Ltd* [2021] EWHC 2086 (Ch) (**Dukeries**), although not binding in Jersey, is of particular note also in that regard. It serves to highlight the importance, as the High Court put it in *Dukeries*, of the need to be "*scrupulous*" in ensuring the Court is given a complete and accurate picture on such applications, including evidence as to the understanding of the effect and consequences of the transaction in question.

Background to the E Settlement

By way of background to the **E Settlement**, the settlor was the sole economic settlor of the Trust. He had an English domicile of origin but later moved to Papua New Guinea and then to Australia. He and his family had Australian citizenship. After separating from his then wife, in 1993, he returned by himself to the UK to manage a substantial family estate that had been in the family for decades but had fallen into disrepair. He subsequently remarried and he and his wife lived in the estate.

On the advice of his accountants, he submitted a domicile application to HMRC to have his Australian domicile of choice accepted and HMRC accepted in 1998 that he was not domiciled in the UK "at present".

When living in Papua New Guinea, the settlor had established himself in the coffee plantation business which became very successful. He established a Hong Kong company called H Limited. He owned shares in that company which owned land in the United Kingdom which was in the process of being sold towards the end of 2007. Around that time, the settlor became aware of the proposed changes to the United Kingdom tax legislation regarding UK resident but non-domiciled individuals and sought advice as to the potential tax consequences for himself as a non UK-domiciled individual.

The settlor was advised that if contracts on the sale of land were exchanged before 5 April 2008, any changes to the capital gains taxation rules would not apply and any gains realised in H Limited would not be attributable to him, whereas there would be taxable gains if the contracts were exchanged after 5 April 2008. He was advised to settle his shares in H Limited into a trust before 5 April 2008 to avoid personal liability for the resulting capital gains tax and mitigate the impact of the anticipated changes to the UK tax legislation and told that the sooner he did it, the less room HMRC would have to query his domicile for inheritance tax purposes.

The settlor was advised that there was no downside to settling the shares into trust before 5 April 2008 when in fact the lawyer advising him at the time ought to have realised that there was a real risk of such a challenge and potential downside if HMRC successfully did so, namely very substantial inheritance tax liabilities.

The settlor's domicile was later challenged by HMRC who said that he had retained his domicile of origin throughout his life, including at the time of the transfer of the shares into the trust. The effect of that, if correct, was substantial inheritance tax liabilities for the settlor, representing approximately one third of the value of the trust. The settlor applied to set aside the trust or the transfer of the shares into the trust on the grounds of mistake, in other words, had he been advised as to the risk of challenge to his domicile by HMRC (and the consequent adverse IHT liabilities) he would not have established the trust and settled the shares onto it.

The Court's decision

While accepting that the question of domicile is not always straightforward, which it confirmed it did not need to determine for the purpose of the application, the Court did comment that it does not think there is much doubt that persons in the position of the settlor would generally be expected to have "a firm grasp of the headline issues – the fact that a person had a domicile of origin, and that he could, by a combination of residence and intention, abandon that domicile and acquire a domicile of choice elsewhere" and that most people in the position of the settlor would be well aware of the fiscal advantages in the UK of being a non-domiciled UK resident.

Having analysed the evidence and in particular the confirmation from HMRC in 1998 confirming the Settlor's non UK domicile "at present" and subsequent advice from his lawyer providing his "immediate comments", the Court said that the Settlor ought to have realised that the legal advice

given at that time about the "all but impossible" prospect of HMRC challenging his domicile was not unequivocal. Noting however the erroneous advice given to the Settlor that there was no downside to proceeding as he did, the Court accepted "with some hesitation" on the evidence and on the balance of probabilities that the Settlor was mistaken as to the possibility of HMRC challenging his domicile and the substantial tax consequences thereof.

In considering whether or not the settlor would have proceeded as he did 'but for' that mistake, after the hearing, the Court invited further written submissions from the settlor on the potential capital gains tax liabilities and savings had the sale of the land gone ahead without the trust being made. The Court made this request because it considered that it might have had a bearing on the mindset of the settlor at the time. If the potential capital gains tax liability were considerably higher than the potential inheritance tax liability, then the Court might have concluded that the settlor might have gone ahead anyway, and that the mistake did not operate on his state of mind and the actions he took. The further submissions and evidence from the settlor, showed that there was no CGT advantage in making the trust. In fact there was a potential CGT disadvantage and the risks of making the trust were identified to be much higher than was originally thought to be the case even at the date of issuing the application. The Court had no difficulty in accepting that the settlor would not have established the trust in 2008 had he not been operating under the mistake he was.

As to the seriousness of the mistake, the Court was satisfied there was no doubt about that. The potential tax liability was very substantial and potentially catastrophic for the settlor and his family with a real risk of bankruptcy for the settlor.

In all the circumstances of the case and on the evidence before it, the Court considered it an appropriate case in which to exercise its discretion and set the Trust aside on the grounds of mistake.

Interesting takeaways

The Court's observation that the settlor ought to have appreciated the unequivocal nature of the advice received, on its face, appears a little harsh but it would appear that the Court is placing a burden on future applicants to ensure that not only have they received professional advice in relation to the effect and consequences of their actions, but that they have interrogated that advice objectively based on the knowledge that they might reasonably be expected to have. It ties into the need to provide evidence as to the understanding of the effects of the transaction

The Court's confirmation that it will expect to be provided with all relevant advice (including privileged advice) or documents, a point not tackled directly in previous cases, is not surprising, it being essential, as the Court observed, to it being able to make a proper assessment as regards whether or not there has been a genuine mistake.

That is a point emphasised by the English High Court case of *Dukeries*, which although not binding in Jersey, is of persuasive value and serves to highlight the dangers of inadequate evidence being put before the Court on such applications.

In *Dukeries*, the High Court dismissed an appeal holding that contributions to the trusts in that case could not be set aside. In *Dukeries*, it became clear that the settlors had not given any real attention to the documents they were signing and what they were meant to achieve. The Court found that if those involved in setting up the trusts in *Dukeries* had not given the documents even a cursory view, it followed that they could not have been mistaken as to the effect. There the High Court considered that the witness evidence relied on had been constructed to make a legal case rather than provide evidence. Evidence as to the understanding of the effects of the transaction in that case was found to be completely lacking and "*positively unhelpful*" to the settlors' case.

Concluding remarks

The cases taken together show that the quality of evidence produced in applications seeking relief on the grounds of mistake (as in so many applications) is key to enabling the Court to carry out a proper assessment as regards whether there has been a genuine and serious mistake but for which the trust or transfers into trust would not have been made.

As the English High Court said in *Dukeries*, when pursuing such an application, whether in Jersey or England, be scrupulous in ensuring the Court is given a complete and accurate picture. What was the understanding as to the effects and consequences of the transaction? Consider the evidence and any gaps in it carefully and whether or not those gaps can be explained. Do not run the risk of failing to adequately prepare. *Dukeries* is a salutary lesson of what will happen if you do.

Rebecca McNulty appeared as Advocate for the settlor in *E Settlement*.

This briefing first appeared in *Trusts and Estates Law and Tax Journal*.

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