UPDATE

SEPTEMBER 2017

mourant

Tax planning disaster – Guernsey court to the rescue setting aside transfer to a trust on grounds of mistake

Update prepared by Chris Duncan (Senior Associate, Guernsey) and Iona Mitchell (Associate, Guernsey)

The Royal Court has recently saved the owner of the successful Slimming World business from transferring the proceeds of her life's work into a tax planning structure which turned out to be fundamentally flawed.

Background

In 2008, upon the advice of professional advisers, the applicant transferred her shares in Slimming World companies into remuneration trusts set up with the purpose of reducing her and her heirs' tax exposure. However, when the applicant instructed new financial advisers in 2016 she discovered that the previous tax advice had been incorrect and the structure would not procure the tax advantages it had aimed to achieve and would in fact have disastrous tax implications. In an attempt to remedy this, the Applicant made an application under section 69(1)(a)(iv) of the Trusts (Guernsey) Law, 2007 (the **Trusts Law**) – which confers wide powers on the Royal Court in Guernsey to make an order in respect of trust property – to have the transfer of the shares into the trusts set aside on the grounds of mistake.

The applicable law

The Royal Court had jurisdiction to determine the matter by virtue of section 4 of the Trusts Law, because the trustee was resident, and the property of the trust was administered, in Guernsey. However, as the companies were incorporated in England, the applicable law to determine the question of whether the transfer should be set aside was that of England and Wales. Expert evidence as to the application of the relevant English law principles of mistake was therefore adduced in support of the application.

The test and tax avoidance

There is a well-developed body of case law relating to the question of whether a transfer into a trust should be set aside on the grounds of mistake. The leading authority in England is the decision of the English Supreme Court in *Pitt v Holt* [2013] UKSC 26, which has recently been followed in Guernsey (in both *Nourse v Heritage Corporate Trustees Limited and Concept Fiduciaries Limited* (Royal Court Judgment 01/2015) and *Gresh v RBC Trust Company (Guernsey) Limited & Anr* (Royal Court Judgment 06/2016)).

The decision of *Pitt v Holt* identified the following principles when considering whether to set aside a transfer on the grounds of mistake:

- there must be a distinct mistake, as distinguished from mere ignorance or inadvertence;
- a mistake may still be a relevant mistake even if it was due to carelessness on the part of the person making the voluntary disposition, unless the circumstances are such as to show that he or she deliberately ran the risk, or must be taken to have run the risk, of being wrong;
- the mistake must be causative and sufficiently grave, and the court must find that it would be unjust or unconscionable to leave the mistake uncorrected; and

- the injustice (or unfairness or unconscionableness) of leaving a mistaken disposition uncorrected must be evaluated objectively but with an intense focus on the facts of the particular case.

The present case is interesting because it deals with the topical and controversial question of whether the court should grant relief where the mistake took place in the context of tax avoidance, which was described in passing by Lord Walker in the *Pitt v Holt* decision as 'a social evil which puts an unfair burden on the shoulders of those who do not adopt such measures'.

Since the English Supreme Court made those comments in *Pitt v Holt*, the courts of both Guernsey and Jersey have considered this question and, although each case will depend on its facts, the message seems to be that tax avoidance (as opposed to tax evasion, which is unlawful) is not of itself a reason to refuse to set aside a transfer on the grounds of mistake. Determining what amounts to a 'social evil' is a complex question, and not one which the Courts should necessarily seek to answer in this context, especially where members of society must be entitled to organise their affairs in such a way so to reduce tax exposure as much as possible within the confines of what is lawful.

The decision

In the present case, the Royal Court distinguished 'artificial tax avoidance transactions', which may justify refusal to grant the relief, and the present arrangement. The Lieutenant Bailiff noted that here there was a genuine transfer of the shares into the trusts, with a genuine trustee, following a remuneration trust structure which has been adopted by many businesses similar to Slimming World. The transfer had been made on the basis of incorrect professional advice, would not have been carried out had the applicant known the true position, and if uncorrected would have meant that the applicant had divested herself of her controlling shareholding in her companies for non-existent tax advantages. Accordingly, the relief was granted and the transfer was set aside. This was not prevented by the passage of some eight years between the creation of the scheme and the discovery of the error.

Given the test set out in *Pitt v Holt* was followed in the recent *Gresh* decision, it is expected that the same result would have been reached had the Royal Court been applying Guernsey law.

The authors would of course be happy to discuss the judgment in further detail and can be contacted using the details provided.

Contacts

Chris Duncan
Senior Associate, Guernsey
+44 1481 739 373
chris.duncan@mourant.com

Iona Mitchell
Associate, Guernsey
+44 1481 731 406
iona.mitchell@mourant.com

This update is only intended to give a summary and general overview of the subject matter. It is not intended to be comprehensive and does not constitute, and should not be taken to be, legal advice. If you would like legal advice or further information on any issue raised by this update, please get in touch with one of your usual contacts. © 2018 MOURANT OZANNES ALL RIGHTS RESERVED