

Trustee's application pursuant to section 69 of the Trusts (Guernsey) Law 2007, as amended, to rectify a Discretionary Trust Deed

[2019]GRC074

IN THE ROYAL COURT OF GUERNSEY

ORDINARY DIVISION

**IN THE MATTER OF THE B TRUST AND IN THE MATTER OF
SECTION 69 OF THE TRUSTS (GUERNSEY) LAW, 2007**

Between:	A	Applicant
	and	
	NERINE TRUST COMPANY LIMITED	Respondent

Judgment handed down: 7 November 2019

Before: Sir Richard Collas, Bailiff

Advocate for the Applicant:	Advocate N Kapp
Advocate for the Respondent:	Advocate A R Lyall

Cases, Texts and Materials referred to in Judgment

OSM Provident Fund [2018] GRC33
BNC v Virtue Trustees [Switzerland] AG [2018] JCA 219
Day v Day [2014] Ch 114
Gamble [2003] GRC 30
Pitt v Holt [2013] 2 AC 108

Introduction

1. This is a Trustee's application ("the Application") pursuant to Section 69 of The Trusts (Guernsey) Law 2007, as amended, (the "Trust Law") to rectify a Discretionary Trust Deed referred to as the "B Trust". The Application was amended by Advocate Kapp on behalf of the Applicant at the oral hearing on 1 November 2019 to substitute a revised trust instrument which is marked as "B (amended)".
2. At a preliminary hearing on 8 March 2019, the Deputy Bailiff ordered that the Application be served on the International Revenue Service in Washington DC, United States of America (the "IRS"). He made Orders relating to the sealing and redaction of materials filed in support of the Application. He also ordered that the Application be heard in public on the basis that no identifying personal or financial information of the Applicant, the beneficiaries, the underlying companies or the B Trust be referred to at the hearing or published in any written judgment to be delivered by the Court.
3. The Deputy Bailiff also ordered that the Advocates for the Applicant and the Respondent propose and deliver to the Court, for its approval, a protocol to maintain the confidentiality of

all identifying, personal or financial information. The protocol they agreed was approved by him on 3 March 2019. In this judgment I will endeavour to refer to the restricted terminology by the replacement terms set out in the protocol.

4. Advocate Kapp appeared for the Applicant who I refer to both as “Mr A” and as “the Applicant”. In the protocol he was also called “the Businessman” which is a slightly misleading title in that his business affairs were largely left to others to whom his affairs were delegated. Advocate Abel Lyall appeared for the Respondent, the Trustee of the B Trust.
5. I had before me one Affidavit from each of: (i) “Mr F”, Mr A’s accountant; (ii) Jeremy Mills, a Notary Public in England and Wales who gave strategic tax planning advice on setting up a trust structure for Mr A; (iii) Mark Biddlecombe, in-house legal counsel of the Respondent; and (iv) Mr A. There were two affidavits sworn by Stephen Nerland, a tax partner at Withers LLP who gave advice that has led to the rectification which is the subject of the Application.
6. I also had an affidavit from Jill E Misener, counsel in Mr A’s US tax attorneys, being the second affidavit sworn by her in these proceedings. She confirmed service of the Application on the IRS, gave evidence of a telephone call with an IRS attorney and of a meeting with IRS counsel. She advised that the IRS had declined to participate in the rectification proceedings and confirmed that receiving rectification in Guernsey is a pre-condition to the IRS recognising that ruling. She said she had been informed by the IRS that it would not automatically follow the Guernsey ruling but would independently review the facts of the case before determining whether the amended trust instrument would be treated for US federal tax purposes as a foreign non grantor trust backdated to the date of inception of the B Trust.

Background

7. The B Trust was created as part of the tax planning Mr A was advised to make when he was contemplating relocating his residence to a State in the USA. Mr A was born in the United Kingdom and was resident there at the time of creation of the B Trust. The evidence before me contains full details of the steps taken by Mr A to obtain advice, details of the professionals who were instructed and the instructions given to each of them prior to his relocation to the USA. It is not necessary for me to set out full details in this judgment. It is sufficient to summarise.
8. Mr A was advised to segregate his global business income into two separate categories: “Active Income” and “Passive Income”. His Active Income would be sufficient to maintain him and his lifestyle whilst resident in the US. He was advised to settle the Passive Income into a trust that minimised his exposure to US tax when he became resident in the US.
9. That could have been achieved through establishing a foreign non grantor trust. The Trust Instrument drafted for him was based upon a standard Guernsey law discretionary trust amended in accordance with the advice received by Mr A. It later emerged that there were deficiencies that result in the B Trust being treated as a foreign grantor trust under US federal tax law. As the settlor or grantor, Mr A is chargeable for US income tax on the trust’s income and gains as if he had earned them personally.
10. The fundamental purpose of the rectification application is to convert the B Trust from a foreign grantor trust to a foreign non grantor trust which, it is submitted, is what is required to satisfy the purpose for which the B Trust was created by Mr A.
11. It is not necessary for me to detail in this judgment all the deficiencies in the drafting. I will highlight just a few. Mr A was incorrectly advised that income could be accumulated within

the B Trust whilst he was US resident but he could be added as a beneficiary later. That was, as Advocate Kapp explained, fundamentally incorrect. In order to satisfy the requirements of a foreign non grantor trust which is treated as a separate entity for US tax purposes, the trust grantor must have no powers or interest in the trust. As a further example, there was nothing within the terms of the B Trust that would prevent Mr A from appointing himself to become a trustee. Furthermore, one of the other beneficiaries is a second trust established by Mr A, referred to as the “C Trust”, which is a foreign grantor trust.

12. In his affidavit, Mr A gave evidence that prior to relocating he wanted to shelter his Passive Income in a trust which would not give rise to US tax. He had no knowledge of US federal tax. He relied upon the professional advice obtained for him and on his behalf by those in whom he entrusted responsibility for his tax affairs. He had intended to divest himself of the assets that were settled into the B Trust so that the income and gains arising therefrom would not be taxable whilst he was resident in the US.
13. The deficiencies in the B Trust became apparent in 2016 when Withers were appointed to give advice. Since then Mr A has been subject to tax investigations in three jurisdictions. The time spent by his advisors in dealing with those tax investigations is the explanation for the delay of two and a bit years in applying to the Royal Court for rectification.

The Law

14. The legal principles that govern the remedy of rectification under Guernsey law are well settled and derive from principles that have been established as a matter of English law and are similar to the principles applied in Jersey. They were set out most recently in the matter of the OSM Provident Fund [2018] GRC33 at paragraph 6 where the Deputy Bailiff held that *“accordingly, in order to succeed in the claim for rectification of a Trust Instrument arising from mistake, an applicant must demonstrate that:*

- (a) there is sufficient evidence that an error has been made so that the document does not carry out the true intention of those involved;*
- (b) to the highest degree of civil probability, a genuine error has been made;*
- (c) there has been full and frank disclosure;*
- (d) there is no other practical remedies; and*
- (e) there has been no undue delay in seeking relief.”*

15. The principles applicable to rectification under Jersey law were set out by the Jersey Court of Appeal in BNC v Virtue Trustees [Switzerland] AG [2018] JCA 219 at paragraph 21, quoting from Lewin on Trusts 19th Edition:

“The conditions which must be satisfied in order for the Court to order rectification of a voluntary settlement are as follows:

- 1. There must be convincing proof to counteract the evidence of a different intention represented by the document itself;*
- 2. There must be a flaw (that is an operative mistake) in the written document such that it does not give effect to the Settlor’s intention;*
- 3. The specific intention of the Settlor must be shown; it is not sufficient to show that the Settlor did not intend what was recorded; it must also be shown what he did intend; and*

4. *There must be an issue capable of being contested between the parties affected by the mistake notwithstanding that all relevant parties consent.*

22. *To these requirements I would add that there must be full and frank disclosure; that no other remedy is available to achieve the same ends; and that even when the requirements for rectification are satisfied the Court retains a discretion whether or not to rectify.”*

16. I see no substantive difference between the two different expressions of the legal test. The test expressed by the Jersey Court of Appeal elaborates somewhat on the test expressed in Guernsey but it is not fundamentally different.

Discussion

17. Mr A was not the immediate settlor of the B Trust which was created by nominees acting on his instructions. If there has been a mistake in that the document does not give effect to the original intention, it is the intention of the principal, not the agent, that has to be identified (see Day v Day [2014] Ch 114). The B Trust was created on the instructions of Mr A, he was the effective settlor. He is also the grantor for the purposes of US federal tax law. It is his subjective intention that is relevant.

18. Mr A’s true intention in causing the B Trust to be created was to divest himself of the assets that produce his Passive Income so that he would not be subject to US Federal Tax whilst resident in the USA. The standard of proof required is that of the balance of probabilities but the documentary and affidavit evidence before me proves convincingly that that was his intention.

19. The way to achieve that purpose was to settle a foreign non grantor trust and for the reasons identified in the expert advice Mr A has now received, the B Trust failed to do so. The evidence is that it would have been lawful for him to have created a foreign non grantor trust, that is to say lawful under the laws of the USA. It would also have been lawful in Guernsey where public policy does not require the Court to protect the interests of a foreign revenue as Carey, B held in re Gamble [2003] GRC 30.

20. Advocate Kapp characterised the mistake as being one of an incorrect tacit assumption by reference to Pitt v Holt [2013] 2 AC 108, paragraph 105. It does not matter that Mr A lacked a knowledge and understanding of the requirements needed for a foreign non grantor trust. Ignorance is not as such a mistake but can lead to a false belief or assumption which the law will recognise as a mistake.

21. There is no other practical remedy available. It is most likely that Mr A would have an action in negligence in respect of the incorrect tax advice he was given at the outset. It cannot be said that would be a more practical remedy. Mr A would no doubt face the defence of failing to mitigate his loss if he had not applied for rectification. I am satisfied that he is not required to pursue a negligence claim indeed a negligence claim might be unsatisfactory because his losses will be on-going and no doubt be difficult to quantify in advance.

22. The legal principles set out above confirm that rectification is a discretionary remedy and any delay in applying for rectification would be a fact for the Court to take into consideration in the exercise of its discretion. The delay in this case is not excessive and can be explained by the pre-occupation of Mr A and his advisors in dealing with the tax investigations in three jurisdictions to which he was subject.

23. The materials before me are comprehensive and have given full and frank disclosure of all relevant facts.
24. In addition to Mr A, the persons affected by the Application include his mother who is a beneficiary of the B Trust and has indicated in correspondence that she supports the Application. The C Trust is another beneficiary but at present it is a mere shell and will become redundant.
25. Nerine, the trustee of the B Trust has appropriately taken a neutral stance.

Conclusion

26. Mr A has satisfied me that the B Trust does not meet the purpose for which it was created and does not give effect to his true intentions. All the legal elements required for rectification are satisfied. There is no reason to refuse the application. I therefore order that the B Trust be rectified in accordance with the Trust Instrument attached and marked "B (amended)".