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UPDATE

When can flawed tax planning be set aside?

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The Royal Court has considered two cases where it was asked to reverse transactions which gave rise to unwelcome tax consequences. In both cases it was invited to do so in accordance with the *Hastings-Bass* principle.

Introduction

At the end of last year, we wrote about the decision of the Royal Court of Guernsey to set aside a flawed transfer into a trust on the grounds of mistake (the Slimming World decision). 'Tax planning disaster - Guernsey court to the rescue setting aside transfer to a trust on grounds of mistake'.

This year, the Royal Court has considered two other cases where it was asked to reverse transactions which gave rise to unwelcome tax consequences, though in both cases it was invited to do so in accordance with the *Hastings-Bass* principle. Notwithstanding some similarities, the two cases resulted in entirely different outcomes, which highlights the sensitive and careful approach required when considering any such application.

The rule in *Hastings-Bass*

Historically, the *Hastings-Bass* jurisdiction gives the Court the power to intervene in and set aside an *act, disposition or transaction made by a trustee in breach of trust, based on the need to protect beneficiaries against* aberrant conduct by their trustees. The exercise of the jurisdiction was considered recently by the Supreme Court in *Pitt v Holt*, wherein the Court, in a decision which narrowed the width of the remedy, observed that it was available in three situations:

1. Where the trustees had gone beyond the copy of their powers in carrying out the transaction/disposition;
2. Where the trustees had acted fraudulently in carrying out the transaction/disposition; or
3. Where the trustees acted within their powers, and not fraudulently, but acted without sufficient deliberation.

Crucially, in *Pitt v Holt* the Court found that in the third scenario, the jurisdiction will only be available if the trustees had acted in breach of duty. It was not sufficient to simply show that they would have acted a different way had they given the matter sufficient deliberation.

In a 2015 decision, the Royal Court of Guernsey confirmed that these principles form part of Guernsey law, albeit the judge in that case did not need to confirm the scope of the jurisdiction. It was also left undecided whether Guernsey would apply the original, wider *Hastings-Bass* jurisdiction or the restricted *Pitt v Holt* version (or indeed follow some other approach, as Guernsey is free to do).

Recent Guernsey decisions applying *Hastings-Bass*

In the first of these cases, *M v St Anne's Trustees Limited*, the Royal Court confirmed that, although not bound by the English jurisprudence, it would apply the revised *Pitt v Holt* version of the test. However, it observed that the Court should not slavishly follow the doctrine, was free to develop the principles and to determine each case in accordance with the specific facts. In particular it warned that it should be careful not to allow the availability of the jurisdiction to be undesirably wide by being quick to find breach of duty on the part of trustees.

The appropriate test is whether or not the court finds it unconscionable that the transaction in question, caused by the trustee's breach of duty, should be left to stand. The Court observed that there are obvious parallels between the operation of the *Hastings-Bass* doctrine, and the equitable relief to set aside a voluntary disposition on grounds of mistake used in the Slimming World decision.

On the facts of the case, the Royal Court refused to invoke the available *Hastings-Bass* jurisdiction in order to undo a transaction which led to an unnecessary tax charge in connection with a pension scheme. Here, the transaction was undertaken at the instance of the beneficiary of the scheme. The trustees had not taken tax advice but advised the beneficiary to do so. The affected beneficiary therefore sought UK tax advice which later turned out to be erroneous.

The Court did not expressly decide whether a breach of duty by the trustees had been made out, but instead found that the application failed on the second limb of the test, namely that it was not unconsciousable for the transaction to stand. Although the size of the unnecessary tax liability naturally provided sympathy for the beneficiary, this alone was not enough. It was open to the affected beneficiary to have taken action against its UK tax adviser, and it was accordingly not unjust to refuse to apply the *Hastings-Bass* remedy.

Conversely, in *Re the Achilles Trust,* the Royal Court granted an order undoing a transaction entered into by the trustees on the basis of the same Hastings-Bass jurisdiction. Here, the trustee was in breach of its duty in failing to consider the consequences of the appointment of the assets. Whilst the written judgment is not yet available, it is understood that important factors (distinguishing this case and its outcome from that in M v St Anne's Trustees Limited) were that the beneficiary had not instigated the transaction in question, and that the trustees had not obtained any tax or legal advice on the consequences of it. Accordingly, the jurisdiction was invoked to protect the beneficiary and the transaction was set aside.

Conclusion

These two recent decisions are a reminder that it should not be assumed that a transaction will be set aside under *Hastings-Bass* principles, even if the result for the beneficiaries of to doing so would be disastrous. The approach of the Court will very much be determined by the facts of each case and will often come down to subtle nuances in presentation and emphasis, in respect of which advice should be sought at the earliest opportunity.

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