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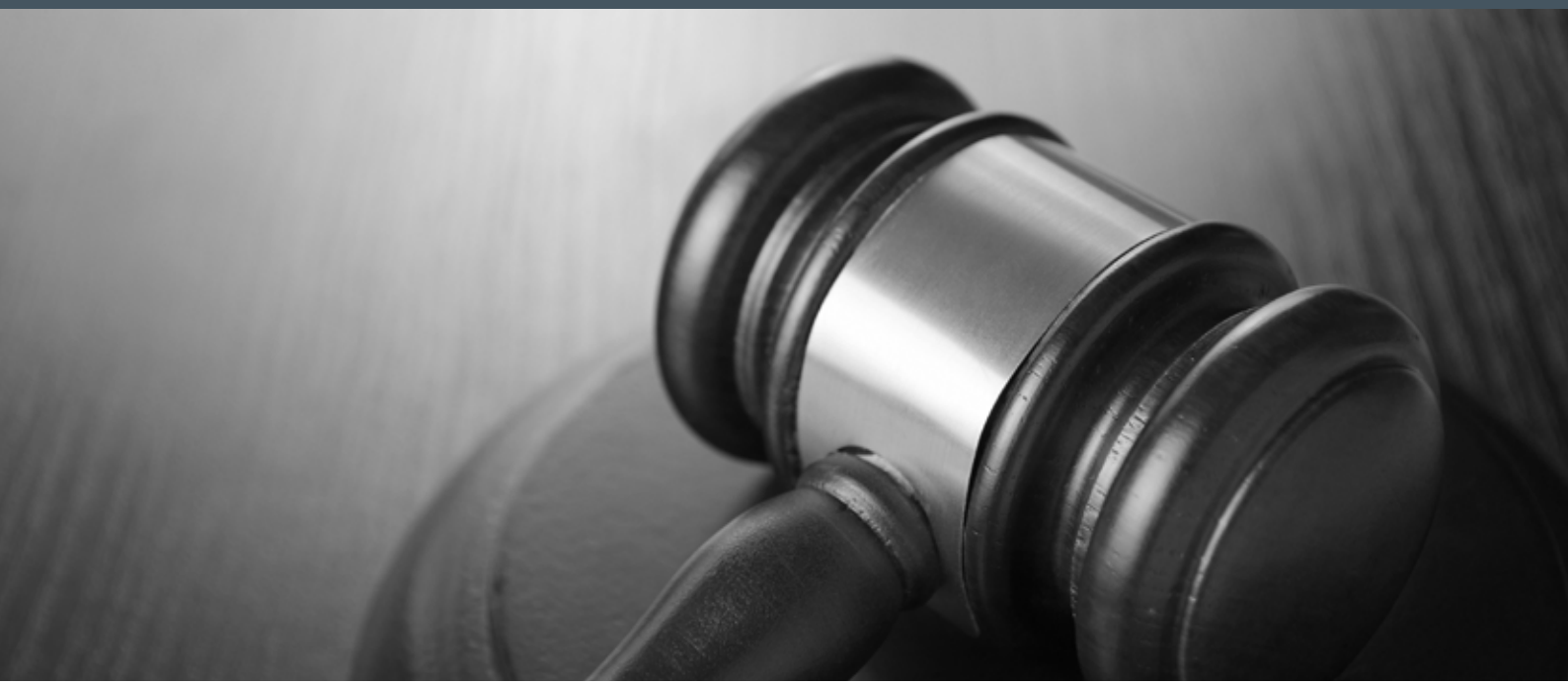

Hastings-Bass: The Diverging Approaches of England and Jersey

Earlier this year the Supreme Court issued its ruling in the linked cases of Futter and Pitt ([2013] UKSC 26) which clarified and, in doing so, restricted 'the rule in Hastings-Bass' which allows trustees to have their actions set aside in certain circumstances. Walker LJ's judgment also included some interesting though strictly incidental remarks about tax avoidance. In a further development last week the Privy Council gave its sanction to Jersey legislation allowing trustees to take advantage of the earlier, and more generous, interpretation of the rule.

Futter: Facts in Brief

The trustees of a number of family trusts made distributions which their solicitors advised would not give rise to a capital gains tax charge. Unfortunately the solicitors were wrong, and a large tax charge fell due.

The Trustees' Argument

The trustees sought to have their actions set aside essentially on the basis that, had they been aware of the tax consequences, they would not have acted as they did. The principle they sought to rely on, commonly known as '*the rule in Hastings-Bass*' (but held by the Supreme Court actually to have had its origins in the judgement of Warner J in Mettoy Pension Trustees Ltd v Evans [1990] 1 WLR 1587) is:

"*Where a trustee acts under a discretion given to*

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him by the terms of the trust, the court will interfere with his actions if it is clear that he would not have acted as he did had he not failed to take into account considerations which he ought to have taken into account."

The trustees contended that they had failed to take into account the tax consequences of the distributions, and so fell within the ambit of the rule.

The Rule in Hastings-Bass - Opening The Door Walker LJ in the Supreme Court echoed the widespread concern that the decision in Re Hastings-Bass ([1975] Ch 25) had "*set ajar a door that was pushed wide open*" in a series of later cases, with trustees taking advantage of a 'soft option' when they had made an error and needed to unscramble an unsuccessful tax-planning arrangement. As Norris J had commented in the judgment at first instance in Futter:

"*This is another application by trustees who...wish to take advantage of this failure to perform their duties in order to enable the beneficiaries to avoid paying the tax liability...Put like that...the possibility is raised that the development of the rule may have been diverted from its true course*".

Closing The Door

In the Court of Appeal Lloyd LJ had held that 'the rule' as employed in the later cases was not a correct statement of the law, and Walker LJ in the Supreme Court concurred. A detailed analysis of the case law revealed that the rule in Hastings-Bass was in fact no more than this: the Court may intervene and declare an act by trustees voidable if the trustees have acted in breach of their fiduciary duty (which requires them to take into account relevant considerations). Over the years the Court had, erroneously, come to believe that the rule applied to cases where there had been no breach of duty, only "*inadequate deliberation*".

Walker LJ held that the Futter trustees had not acted in breach of their fiduciary duties. They might have been in breach if they had given no, or hardly any, thought to the implications of their actions. But in fact they had taken advice from an appropriate source (their London solicitors) and had acted on that advice; they had thereby discharged their duties. It just so happened that the advice they had received was wrong.

Rather archly, particularly given the current political emphasis on tackling tax avoidance, Walker LJ also commented:

"*It might be said...that the greater danger is not of trustees thinking too little about tax, but of tax and tax avoidance driving out consideration of other relevant matters*".

The Supreme Court concluded that, in the absence of a breach of fiduciary duty by a trustee, the Court had no jurisdiction to intervene. In acting on the advice they had received, the Futter trustees had committed no such breach, and their appeal against the Court of Appeal decision was dismissed. Time will tell whether the next step is a claim against their solicitors for professional negligence.

Pitt: Facts In Brief

This case turned on the related but distinct legal doctrine of mistake. Mrs Pitt had been advised that settling a considerable amount of money into a trust for the benefit of her husband, who had been disabled in a car accident, would have no inheritance tax consequences. However, the trust which was eventually prepared was not of the correct type, and so a large inheritance tax charge fell due. Mrs Pitt's executors sought to have her gift into trust set aside.

When the Court will 'Unmake' a Mistake

The courts have usually drawn a fine distinction between the legal effect of an action and its other (i.e. tax) consequences, and declined to give relief on the basis of a mistake relating only to the latter. The Supreme Court disagreed with this approach. Walker LJ held that the Court should simply focus on and evaluate objectively the "*gravity of the mistake*" and "*its consequences for the person who made the vitiated disposition*". Having considered the matter

in the round, it should "*make an evaluative judgment whether it would be unconscionable, or unjust, to leave the mistake uncorrected*". In this case it would have been unjust not to reverse the mistake, and so relief was granted.

One result of the judgment appears to be that if trustees take a step, and their decision to do so is based on incorrect advice concerning its tax consequences, relief may be available on the basis of mistake but not under the rule in Hastings-Bass.

And How Will The Court Treat Claims Involving Tax Avoidance 'Schemes'?

While Walker LJ's conclusions are based solely on legal principle, it is worth noting that he made further comments about tax avoidance in the later parts of the judgment. There was nothing '*artificial or abusive*' about Mrs Pitt's trying to take advantage of the tax reliefs offered to trusts for disabled persons, and this evidently assisted the Court in finding that it would be '*unconscionable*' to leave her mistake uncorrected. By contrast, while "*The scheme adopted by Mr Futter was by no means at the extreme of artificiality...it was hardly an exercise in good citizenship*".

Walker LJ appeared to be laying down a marker for the future when he said: "*Had [the doctrine of] mistake been raised in Futter there would have been an issue of some importance as to whether the Court should assist in extricating claimants from a tax-avoidance scheme which had gone wrong*", his clear implication being that it should not.

Futter and Pitt in Jersey

The decisions of Futter and Pitt were considered by the Jersey Royal Court in Re the B Life Interest Settlement [2012] JRC 229 and In the matter of the Onorati Settlement [2013] JRC 182. In neither case was it necessary for the Court to decide whether to follow the developments in English law. However, in Onorati, Sir Michael Birt, Bailiff said that:

"*any party wishing to submit that Jersey law should continue to plough its own furrow will have to explain why the closely reasoned judgments of Lord Walker and Lloyd LJ should not be applied.*"

To date the Jersey courts have been of the opinion that the clarified and restricted rule in Hastings-Bass should apply to trustees. In the background, however, there has for some time been a proposal to make the rule in Hastings-Bass, as it has traditionally been understood, part of Jersey legislation. The draft legislation (Trusts (Amendment No 6) (Jersey) Law 2013), received the sanction of the Privy Council last month. It provides that the courts may set aside an exercise of a power relating to trust property where the person exercising the power failed to take into account relevant considerations (or took into account irrelevant considerations) and, had they taken into account the correct considerations, would not have exercised the power in that way.

The legislation also expressly provides that "*It does not matter whether or not [the failure to take into account the correct considerations was] as a result of any lack of care or other fault on the part of the trustee...or on the part of any person giving advice*".

In other words, trustees may have their actions set aside regardless of whether they have breached their fiduciary duty.

As the legislation does not expressly replace the rule in Hastings-Bass, there is scope for the rule, as developed by Futter and Pitt, to retain a place in Jersey jurisprudence, although how the two can co-exist remains to be seen.

Conclusion

The Supreme Court judgment in Futter and Pitt was impressive and soundly reasoned, putting an end to the uncertainty arising from an ambiguous 'rule'. Where trustees have relied on professional advice, it puts the blame for errors, and therefore the obligation to make reparation, firmly where it should be: on the advisers giving the inadequate

advice. However, this may be of little comfort to beneficiaries: it is easier said than done for a trustee to bring a negligence claim against an adviser, as such claims are expensive, time consuming and by no means straightforward.

A clear message has also been given to trustees caught up in tax avoidance schemes which have gone wrong: in such situations the English Court is unlikely to look favourably on claims under the alternative ground of mistake.

Despite judicial comment in Jersey on the English position, that jurisdiction has enacted legislation preserving the old 'rule' and its 'get out of jail free' card for trustees. This will inevitably be seen as an attempt to protect settlors, beneficiaries and also, crucially, trustees and their advisers, who form an important part of the Island's economy.

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