Wealth and trusts quarterly digest

May 2017

Our quarterly digest provides up to date commentary and analysis on key sector developments. Our tax, wealth and trusts teams are able to provide a wide ranging service to assist you and your clients in responding to market trends and legal developments. We would welcome the opportunity to discuss any issues you may have and always welcome feedback on the content of our publications.

Feature

Making beneficial ownership transparent

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Any comments or queries?

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Case reports

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Making beneficial ownership transparent

Following a public consultation in 2016, the Cayman Islands have published draft legislation to increase transparency in relation to the ownership of Cayman companies by maintaining beneficial ownership registers. This forms part of an ongoing international initiative to address the extent to which companies and trusts are involved in tax evasion, or other criminal activity.

In recent years, there has been a greater focus on offshore jurisdictions, for example the leaked records held by the Panama-based law firm Mossack Fonseca (the so-called "Panama Papers"), has concentrated attention on greater transparency. International initiatives to prevent tax evasion have hitherto concentrated mainly on the exchange of information as regards taxable income[1]. However, particular focus is now concentrated on the provision of beneficial ownership information as a means of preventing corruption and tax evasion by identifying who benefits from, and controls, individual companies.

Beneficial ownership registers

In April 2016, the UK became the first country to introduce a public beneficial ownership register, forcing company owners to provide details such as their name, date of birth and nationality. Whilst the register applies to UK companies, it does not extend to companies registered in British overseas territories and Crown dependencies.

As a result of this, and at the same time as the public beneficial ownership register was introduced, the UK government agreed with British overseas territories and Crown dependencies that there would be a rapid sharing of beneficial ownership information in relation to corporate and legal entities incorporated in their jurisdictions. The Cayman Islands Legislative Assembly has now published draft legislation which seeks to implement this arrangement and bring into effect a searchable, corporate ownership register.

The proposed amendments to the Companies Law, Limited Liability Companies Law and Companies Management Law in the Cayman Islands, provides for an electronic platform to be established. This will require Cayman companies to maintain beneficial ownership registers and for the information on the register to be made automatically available to the Cayman Islands competent authority. The UK authorities, such as HMRC, will be able to request of the Cayman authority that it carries out a search. In future, other jurisdictions entering into similar agreements with the Cayman Islands may also be able to request such a search.

The new regime will align the Cayman Islands with the UK in respect of the beneficial ownership issue and reflects similar international initiatives, including the Fourth Anti-money Laundering Directive in the European Union, which is to be implemented by EU member states by June 2017.

Contents of the register

The beneficial ownership register must contain details of each individual who is the ultimate beneficial owner of the company concerned.

1. For example, beginning from dates in 2017 or 2018 the Common Reporting Standard will see more than 100 countries automatically exchanging information on taxpayers' banks and other financial accounts, with some 30 further countries exchanging information on request.

The details to be included on the register include, name, residential address and (if different) address for service of notices, date of birth, identification information and the date on which the individual became a registrable person.

Failure to maintain the register

If a company fails to maintain the register or keep it up to date (the register must be updated within one month of any changes), and fails to respond to a notice from its corporate services provider requiring it to do so, the company must issue a restriction notice over the shares. A restriction notice will prevent the transfer of, or acquisition of, additional shares and suspend any rights exercisable in respect of the shares eg voting rights. Companies that knowingly and wilfully breach their obligations face penalties including fines and imprisonment. A director, manager, or other officer of the company may face imprisonment where it is proved that an offence was committed with the consent, or due to the wilful default, of the director, manager or other officer of the company. A one-year transitional period has been proposed, from the date on which the law comes into force, after which prosecutions may be brought.

Next steps

The proposals are expected to pass through the usual approval process in the Cayman Islands shortly, after which a date for the new law to take effect will be confirmed.

The Cayman government has previously indicated that it intends to introduce the registers and platform by the end of June 2017. It is clear that the Cayman government is committed to providing UK law enforcement and tax agencies with access to beneficial ownership information. Individuals and companies should prepare for these changes which are likely to take effect within the next few months.

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News

CRS – reporting clients' financial information

In recent years, we have witnessed a shift in the compliance and reporting requirements of the offshore financial services industry. This is seen not least in the new obligations to report clients' financial information to multiple jurisdictions around the world.

The Foreign Account Tax Compliance Act (FATCA) is now well established and the even more onerous Common Reporting Standard (CRS) has been embraced by the likes of Guernsey, Jersey, the UK, and 51 other jurisdictions as "early adopters". These countries will report calendar year 2016 information by 30 June 2017, while a further 47 jurisdictions have committed to the CRS for calendar year 2017.

Participating jurisdictions will implement CRS in a number of different ways and the obligations on reporters may differ greatly depending on which jurisdiction they are in.

The procedures followed in relation to FATCA, have provided businesses with a good foundation on which to implement CRS. However, although procedures and definitions are similar to those relating to FATCA, CRS contains some key differences and covers many more jurisdictions.

It is important that firms document CRS procedures and ensure that staff are aware of CRS requirements while not forgetting that FATCA reporting will continue for US clients alongside this new global standard. The USA has not committed to CRS and most commentators believe they will continue on a FATCA only basis for the foreseeable future.

One peculiarity of CRS for trusts is that protectors, regardless of how wide or limited their powers may be, are reportable as controlling persons. This leads to the unusual situation of an individual with no beneficial interest in a trust having the entire trust balance reported under his name to the jurisdiction in which he is tax resident.

CRS obligations have resulted from the drive towards increased transparency in a globalised financial services environment. Those affected by CRS would be well-advised to ensure that they are fully familiar with its requirements.

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Cayman Islands tightens regulations governing financial institutions under CRS

The Cayman Islands government has announced a tightening of the regulations governing financial institutions' due diligence and reporting obligations under CRS. The amendments made by the Tax Information Authority (International Tax Compliance) (Common Reporting Standard) (Amendment) Regulations 2016 (the Regulations) will allow the Cayman Islands to satisfy the "effective implementation" criteria used by the European Commission when deciding to classify countries as "non-cooperative for tax purposes".

The key changes made by the Regulations are:

- all Cayman Financial Institutions, whether classified as Reporting (RFI) or Non-Reporting (NRFI), must submit a CRS notification to the Cayman's Department of International Tax Co-operation using the Cayman Automatic Exchange of Information online portal (AEOI) by 30 April 2017
- all RFIs must file returns via the AEOI for all reportable jurisdictions by 31 May 2017, even those for which there are no accounts. In the latter case they must file a nil return
- all RFIs must establish written procedures and policies to ensure compliance with the Regulations
- the introduction of various new offences for breach of the Regulations. The maximum penalty for any such offence has been increased from $6,000 to $60,975, and directors and officers may incur criminal liability where they fail to prevent a breach by their financial institution.

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Offshore penalty regulations made

Anyone who has an interest in assets which are located outside of the UK may be affected by recent regulations which the UK government has published which mark the start of a series of changes to the offshore penalty regime[2]. Legislation has been introduced into the Finance Act 2016, which introduces an asset-based penalty for serious cases of offshore tax evasion.

The new regulations, which took effect from 1 April 2017:

- provide that unprompted disclosures may receive a 50% reduction in penalty and prompted disclosures may receive a 20% reduction in penalty
- identify the type of penalty that may be reduced. Penalties for inaccurate returns, late returns and failure to notify a liability relating to an offshore matter, or offshore transfer, have the capability of being reduced and
- specify what information will qualify as disclosure for the purposes of reducing penalties. Such information comprises informing HMRC about the involvement of an enabler, providing HMRC with the enabler's contact information and a description of their conduct. The additional information also involves the disclosure of information relating to beneficial and legal ownership of oversees assets.

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2. The Asset-based Penalty for Offshore Inaccuracies and Failures (Reductions for Disclosure and Co-operation) Regulations 2017 and The Penalties Relating to Offshore Matters and Offshore Transfers (Additional Information) Regulations 2017 (SI 2017/345).

Case reports

Patricia Marigold Bullard v William Harry Bullard and Another[3]

The claimant was the settlor and one of the trustees of a so-called "double trust", in respect of her house, which she understood to create (1) a life interest trust for herself and (2) an interest in possession trust for other beneficiaries. The house was transferred to the first trust, and the resultant debt was assigned to the second trust. The claimant was advised that if she did this there would be no charge to inheritance tax on the property at the outset and if she survived at least three years, inheritance tax on her death would be mitigated, and after seven years avoided altogether.

The beneficiaries of the second trust were the claimant's children and grandchildren, and included the defendants. None of these beneficiaries were adults at the time the trust was created and as a result the interest in possession trust was caught by section 31, Trustee Act 1925 (TA 1925). That section operates to divest the vested interest of a minor in trust property and replace it with a contingent interest in accumulations of income not paid to or applied for the benefit of the minor beneficiary, to be held for that beneficiary contingently upon attaining the age of majority.

The result of this divestiture was that the second trust was not an interest in possession trust for the purposes of avoiding an immediate charge to inheritance tax.

When this came to the claimant's attention, she applied for an order determining the construction of the trust deed, or alternatively a rectification of the trust deed.

Held

Construction of the trust deed

As a matter of construction, the interests of the minor beneficiaries were divested by the operation of section 31.

Section 31 is capable of being modified or excluded under section 69(2), TA 1925, by the trust instrument, but this was not done in this instance. The draftsman of the trust had included a schedule with an express provision applying section 31. This was evidence of the intention of the draftsman, and, on the face of it, of the settlor, that section 31 should apply, notwithstanding the description of the trust as an interest in possession settlement and the effect of that section on the minors' interests.

Rectification of the trust deed

The Court referred to *Re Butlin's ST*[4], in which the judge stated that rectification is available, if certain conditions are satisfied, where "the words of the document were purposely used but it was mistakenly considered that they bore a different meaning from their correct meaning as a matter of true construction".

The necessary conditions, as expressed in *Giles v Royal National Institute for the Blind*[5] were fulfilled, namely:

- there was "convincing proof" that the claimant intended to create an interest in possession settlement to avoid an immediate charge to inheritance tax. This proof came in the form of the claimant's own evidence, that of her former advisor, the fiscal context, and the description of the trust on its face

3. [2017] EWHC 3 (Ch).
4. [1976] Ch 251.
5. [2014] EWHC 1373 (Ch).

- the claimant had executed a deed which she was assured would create an interest in possession settlement. She was not an expert in the field, and could not know the true effect of including section 31. *Butlin* provided that rectification was available where there was a mistake as to the meaning of words. The claimant had in fact made a mistake as to the legal effect of the words, rather than their meaning. However, the court was satisfied that it had the power to rectify the trust deed in these circumstances
- there was clear evidence of the claimant's precise intention, which was to create interests in possession for all the beneficiaries, with section 31 excluded
- there was a real issue as to the beneficial interests. The interests taken by the minors under the trust deed were contingent, but were intended by the claimant to be absolute.

The court therefore granted rectification of the trust deed to exclude section 31.

Comment

This case confirms that the courts may be willing to rectify a trust deed, even to remove express clauses, in order to give effect to a settlor's true intentions provided certain conditions are satisfied.

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Rbc Trustees (Ci) Ltd and Others v Janatha Stubbs and Others[6]

The claimants were the trustees of a settlement who applied to the Court for the rectification of two deeds of revocation and appointment on the ground of mistake. The settlement had been established by deed in 1964 and in 1991 a deed of revocation and appointment provided for settled shares to be held on trust for each of the settlor's three children (A1, A2 and A3).

An additional deed was created in May 2004, which created successive life interests in favour of the spouses of A1 and A2. This ensured that if either of the children in question died, their respective shares would pass to their spouses without liability to inheritance tax.

In 2007 and 2013, the marriages of A1 and A2, respectively, broke down. Two deeds were therefore created in 2008 and 2014, which had the effect of not only severing the spouses' life interests, but also revoking the 2004 appointment (with respect to A1 and A2's settled shares), and reappointing the life interests of the settlor's children, resulting in significant and highly unfavourable tax consequences.

The trustees asked the Court to rectify both deeds, arguing that both the 2008 and 2014 dead had mistakenly, and for no purpose, revoked and reappointed the trusts in relation to A1 and A2, rather than just revoking the former spouses' life interests.

Held

The Court was satisfied that, in accordance with *Racal Group Services Ltd v Ashmore*[7] there was:

- clear evidence of the trustees' subjective intention. The trustees' instructions to their solicitors in 2008 and 2014 were to draft suitable deeds to remove spouses from the beneficial interest. No mention was made to revoking the 2004 appointment
- a flaw in the document so that it did not give effect to the intention. Both deeds were flawed as they made changes to the arrangement of the trust that was not intended

6. [2017] EWHC 180.
7. [1995] STC 1151.

- a specific intention to achieve something different to what had actually been achieved. The only intention was to revoke the former spouses' interests and
- an issue being capable of being contested, namely, being whether the interests of the settlor's first two children (and their respective children) and remoter issue, arose under the 2004 deed or under the 2008 and 2014 deeds.

The Court granted the application.

Comment
This is another example (see also the *Bullard* case reported above) of the courts being prepared to rectify deeds provided certain conditions are met.

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Laurel Marilyn Roberts and Another v Luanne Fresco[8]

The Court has found that a potential claim under the Inheritance (Provision for Family and Dependants) Act 1975 (the 1975 Act) by a surviving husband against his deceased wife's estate abated on the death of the husband.

Background
Pauline Milbour died in 2014 leaving her husband, Leonard, a legacy of £150k and a life interest, or right to income, in £75k, from an estate worth some £17m.

Leonard died shortly after Pauline, leaving an estate worth £320k (including the £150k legacy from Pauline's estate) to his daughter and granddaughter (the claimants).

The claimants applied for permission to bring a claim under the 1975 Act, which Leonard himself had not been able to bring prior to his death.

The claimants contended that both *Whyte v Ticehurst*[9] and *Re Bramwell (Deceased)*[10], had been wrongly decided and that the reasoning behind the judgments had been superseded by Article 1 of Protocol 1 of the Human Rights Act 1998, which provides that "every natural or legal person is entitled to the peaceful enjoyment of his possessions". They also argued that there was nothing in the wording of the 1975 Act itself to suggest that claims could not in principle be brought after the applicant's death, particularly in the case of a claim by a spouse which was not limited to reasonable financial provision for his maintenance.

Held
The Court was not convinced by the claimants' arguments and held that Article 1 of Protocol 1 of the Human Rights Act 1998, did not apply, as Leonard's estate was neither a natural or legal person and therefore *Whyte* and *Re Bramwell* remained good law.

Although the claimants were correct that the wording of the 1975 Act did not, of itself, expressly preclude a claim being brought by the estate of a person who before his death fell within the definition of a person who could bring such a claim, had it been intended that a claim under the 1975 Act should survive for the benefit of the estate of a potential claimant, the statute would have expressly so provided.

Accordingly, the Court held that a claim under the 1975 Act did not survive the death of the applicant.

8. [2017] EWHC 283 (Ch).
9. [1986] Fam 64.
10. [1988] 2 FLR 263.

Comment

It is a well-established principle that claims for financial provision from a deceased person's estate under the 1975 Act do not survive the claimant. Thus, where a claimant who has brought a claim under the 1975 Act dies before trial, unlike many other claims, their personal representatives cannot continue their claim on behalf of their estate. It is not surprising therefore that the Court dismissed the claim given that Leonard had not even started a claim under the 1975 Act at the time of his death.

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