



February 2019

Welcome to our new look Spotlight. Our quarterly update highlights developments in the private client world – with a focus on disputes and how to avoid them. This edition has a decidedly digital feel; we look at how cryptoassets are taxed and blockchain in the art market. We also explore how disgruntled would-be beneficiaries can challenge a will. If you have any feedback on this update or would like to know more about the issues covered, or anything else, get in touch.

The big question

Will blockchain dominate the art world in 2019?

Provenance of artwork has traditionally been recorded on a notoriously piecemeal basis. As pieces of art travel between the creator, galleries, auction houses and private collections, separate records are created at each step, leaving an inconsistent trail of ownership which is vulnerable to forgery.

As a result, RPC often sees disputes arise as to the provenance of artwork, culminating more frequently in restitution – a remedy granted by the courts which restores a piece of art to its rightful owner, where proof of unjust enrichment at their expense is established. The introduction of blockchain in the art world looks set to standardise provenance records, though it is too early to tell whether it will reduce the prevalence of claims seeking restitution.

Restitution – a popular remedy in provenance disputes

Restitution is a growing danger for art buyers. In the United States, the Holocaust Expropriated Art Recovery Act 2016 (HEAR Act) effectively extended the limitation period for Nazi-looted restitution claims and requires the return of property where there is “reasonable proof” of a rightful owner. In April 2018, in one of the first cases under the HEAR Act, a New York judge ruled that two artworks by Egon Schiele should be returned to the heirs of Fritz Grunbaum, a Jewish art collector. There was considerable evidence that the new owner knew of the heirs’ claims before purchase – the new owner had specifically named the heirs in the title insurance.

Meanwhile in Europe, Christie’s was accused of failing to investigate the provenance of a looted painting by Alfred Sisley. The artwork had been stolen from a bank safe in Paris by a Nazi official after its Jewish owner fled the city. Mondex, a Canadian expert in looted art, identified the painting in the Einsatzstab Reichsleiter Rosenberg (ERR) database, an inventory of looted or stolen artworks, and contacted the heirs of the original owner. The dealer who bought the painting at auction in 2008 was promised to return it to the heirs, but is suing Christie’s for its value, arguing that the auction house had access to the ERR database and should have checked it before the sale.

Blockchain in the art market

The art world is now beginning to look to technology as a way of standardising and fortifying provenance records. In particular, blockchain technology offers a system through which data relating to ownership can be stored on a secure centralised system, without the risk of interference, deletion or corruption. A blockchain could in theory act as an impermeable art registry, accessed only by those who have been provided with the means of unlocking it. All information relating to an artwork – including the historic provenance – could be easily accessible, helping to resolve provenance or authenticity disputes.

However, a key challenge in the adoption of blockchain is the question of verification: if incorrect or corrupt information is added to the blockchain in the first instance, the value of the blockchain vanishes. Multiple blockchains, many of which are not connected, mean that we may also see inconsistent platforms or registers appearing simultaneously. Moreover, the technology is far from user-friendly at present; those wishing to buy or sell art must first acquire a “digital wallet” and pay an upfront charge to engage with the network, all the while navigating ever-changing technical jargon.

Despite these obstacles, in November 2018 Christie’s set a new milestone when it raised a total of \$317,801,250 for its sale of the Barney A. Ebsworth collection, the most valuable art auction to ever be recorded on a blockchain. The blockchain (known as The Registry) logs all significant information in the life cycle of an artwork, including sales, auction dates, item titles, restorations and thefts. Ahead of the auction, potential buyers were able to log on and view the entire transaction history of an artwork before bidding, reportedly bolstering buyer confidence.

Given the pace at which progress is being made in this area, it looks like 2019 will be the year that blockchain takes hold in the art market, though whether it will diminish the prevalence of claims seeking restitution of artwork remains to be seen.

What's new?

Executors not entitled to costs of resisting removal where they acted unreasonably

Executors have been ordered personally to pay the costs they incurred resisting their removal. The case of *Griffin v Higgs & Ors*¹ highlights the importance of executors and trustees taking advice before resisting removal or becoming involved in litigation because, as this case demonstrates, they will not necessarily be able to recover their costs from the estate or trust fund.

In *Griffin* a daughter alleged that assets had been transferred from her mother's estate under undue pressure. She applied for the executors to be replaced by an independent administrator on the basis they did not have the necessary independence to investigate the allegations fairly. The executors actively opposed their removal, but then dropped their opposition to the application shortly before the hearing.

The executors were not entitled to recover their own costs from the estate for the period in which they resisted removal, and were also ordered to pay the daughter's costs during this period, because they had acted unreasonably in defending the claim.

So whilst the general principle is that an executor or trustee has the right to be indemnified by the estate or trust for costs incurred on its behalf in court action, this will only be ordered by the court if a trustee or executor has acted reasonably in the claim and their costs were reasonable in amount and reasonably incurred. An executor who is unsuccessful in court action may also be ordered to pay the costs of the other party to the claim.

To increase their chances of recovering their costs from the estate or trust fund and minimise the risk of being ordered to pay another party's costs, executors and trustees could choose to take a neutral stance in litigation. A trustee may ask the court for a "Beddoe" order, in which a court approves the trustee's proposed steps in litigation so giving the trustee certain costs protection.

Notes

1. [2018] EWHC 2498 (Ch)

What's new?

Plans to extend the Trust Registration Service

HMRC launched the Trust Registration Service in 2017. Trustees of “relevant taxable trusts” are required to provide the HMRC Trust Register with details of a trust’s beneficial owners and assets. HMRC guidance sets out which trusts must currently be registered, the information to be provided to HMRC and the records trustees should keep about the trust and its finances. Following the passing of the Fifth Money Laundering Directive (5MLD) on 9 July 2018, many more trusts are set to fall within the scope of the reporting requirement.

Currently, only express trusts with a tax consequence must be registered. A tax consequence means the trust has incurred a liability to pay income tax, capital gains tax, inheritance tax, stamp duty land tax or stamp duty reserve tax.

5MLD removes the tax consequence test. Under 5MLD, all UK resident express trusts and certain non-EU resident express trusts will be required to register. This could include trusts connected with financial products, such as life or shareholder protection policies, and non-EU resident

trusts that own UK real estate or that have a business relationship with an entity obliged to carry out customer due diligence in the UK. When the UK implements these new registration requirements (which it must do by 20 March 2020) many more trusts, and offshore trusts in particular, will be required to register.

The UK Association of Taxation Technicians has calculated that there is likely to be a ten-fold increase in the number of trusts required to register when the new rules are implemented. We will keep you posted with any developments and in the meantime trustees of trusts which may be caught by 5MLD should start considering what the change will mean for them.

What's new?

Anti-money laundering regulations – all change in the art sector

The art world's status as the last unregulated market looks set to change. The Fifth Money Laundering Directive isn't only going to impact the scope of trust registration obligations. It will also affect those selling art for €10,000 or more, regardless of the method of payment.

In RPC's recent article, we considered the likely practical effects of these regulations on the art sector, including the requirement to verify customers and their identities, the introduction of paperwork in a notoriously unbureaucratic sector, and the impact on online purchases. The article also considers implementation of the regulations alongside other existing guidelines in the EU, and the creation of guidelines elsewhere including in the US.

Click [here](#) to read RPC's article on anti-money laundering legislation in the art market.

RPC asks

How are cryptoassets taxed?

The market for cryptoassets has exploded in recent years with hundreds of cryptoassets, such as Ethereum and Bitcoin, now available to use as methods of payment. These present unique regulatory difficulties, not least in the field of taxation. In December 2018, HMRC released guidance as to how individuals should be taxed when handling these cryptoassets.

The key message from HMRC's guidance is that those already using cryptoassets should keep detailed records in order to calculate any tax liabilities accurately. A copy of the guidance can be found [here](#).

Which tax applies?

Cryptocurrencies are commonly held as a personal investment and will therefore be subject to capital gains tax (CGT) on disposal. Individuals will also be liable to pay income tax and national insurance contributions (NICs) on cryptoassets which are received from an employer or income tax on such assets received as payment for a service or which are traded for profit.

Income Tax

HMRC taxes cryptoassets based on the activity of the holder eg. if the holder is conducting a trade, income tax will apply to trading profits.

- Income tax will apply to the profits generated by trading cryptoassets and the individual will be able to offset any losses against future profits.
- If an individual receives a cryptoasset as payment for a service and is not classified as a trader, the profits will be taxed as miscellaneous or other taxable income.
- Where an employee is paid with cryptoassets the individual will need to account for both national insurance and income tax.

Capital Gains Tax

Cryptoassets may be treated as a personal investment and will therefore attract CGT on disposal rather than income tax. HMRC has taken a broad approach to the question of what constitutes a disposal:

- the sale of cryptoassets for money
- giving away cryptoassets
- use of cryptoassets to pay for services, and
- exchanging cryptoassets eg Bitcoin for Ethereum.

The hardest part of the CGT puzzle can be working out an individual's liability. In order to make sure tax liabilities are worked out correctly, HMRC recommends a stringent record is kept of each transaction.

HMRC's guidance notes that the following information makes for useful records for CGT purposes:

- the type of asset
- the date of disposal
- the number of the currency disposed and retained
- the value of the disposal or acquisition in sterling
- relevant bank statements
- wallet addresses
- a record of the pooled costs before and after disposal.

As with income tax, the usual CGT rules apply and individuals may set expenses off against realised gain.

What next?

As cryptoassets become more common HMRC is likely to expand its guidance to take account of the inevitable complexities arising from taxing this type of asset. In the meantime, holders of cryptoassets should keep detailed records and take advice if they are unsure of the scope of their tax liability.

RPC asks

Has a disappointed beneficiary any options?

What are the options available to an individual who has been left out of a will or is otherwise dissatisfied with the will's provisions? In our last update we considered how the validity of a will can be challenged. In this edition we focus on who can apply to the court for reasonable financial provision from the deceased's estate if they have not been properly provided for either in a will or by the intestacy rules². This regime has come into focus in recent years as the court controversially awarded a 50 year old woman a legacy from her mother's estate, despite the fact they had been estranged for some years and her mother had chosen to leave her estate to three animal charities³.

Who can apply?

A broad range of individuals can apply for financial provision from the deceased's estate, whether or not they have already received a legacy through a will (or through intestacy):

- a surviving spouse or civil partner (including a former spouse or civil partner who has not remarried)
- an unmarried partner of the deceased who lived in the same household as the deceased for the two years before their death
- a child of the deceased or someone who was treated as a child of the family
- any other person who was being "maintained" by the deceased, ie the deceased was making a substantial contribution towards the reasonable needs of that person.

What does the applicant need to show?

In order to make a successful application, an individual must show that the will (or intestacy) did not provide them with reasonable financial provision for their maintenance. The applicant must demonstrate that it is objectively unreasonable for them not to receive greater provision. It is not enough to argue that it was "unfair" that they did not receive anything or very much.

What factors will the court consider?

- The financial resources and needs that the applicant and beneficiaries have and are likely to have in future.
- Any obligations and responsibilities the deceased had towards the applicant or any other beneficiary.
- The size and nature of the deceased's estate.
- Any disability of the applicant or beneficiary.
- Any other matter, including the conduct of the applicant or any other person, which the court considers relevant.

There are also factors which the court must take into account which are specific to particular types of applicant. For example, if the applicant is a spouse or civil partner then the court takes into account the age of the applicant and the duration of the marriage or civil partnership. Spouses and civil partners do not need to show that reasonable financial provision is required for their maintenance. This is to avoid a situation where a spouse is better off following a divorce (where they may receive more in a settlement than is strictly required for their maintenance) than on their partner's death.

What can the court award?

The court has broad powers and can award payments of capital or income, transfer property to the applicant and set up trusts.

The rules in practice

Whilst it is fairly clear what the court should consider and what it can do when an individual makes an application for reasonable financial provision, two recent cases demonstrate that multiple parties can have strong claims to a deceased's estate and balancing these competing interests can be a difficult exercise.



The estranged daughter

The general consensus before the case of *Illott v The Blue Cross and others*⁴ was that adult children were unlikely to receive any assistance from the court unless they had a disability or there was some reason why it was unreasonable that they were not provided for in the parent's will. For example, the court had rejected a claim by a son who lived in comfortable circumstances for funds from his father's estate to pay off his mortgage⁵.

In *Illott* an adult daughter had been estranged from her mother for 26 years and was dependent on state benefits. Her mother had completely left her daughter out of her will and had instead left her estate to three animal charities, making it clear that she did not want her daughter to receive anything from her estate.

Despite their sour relationship, the daughter was awarded just under 30% of her mother's estate to purchase her own home (her overall award was reduced to just over 10% on appeal). Following *Illott*, it is generally accepted that claims by adult children who are otherwise able to support themselves are now more likely to succeed.

The unmarried partner

Following *Illott*, the courts were faced with another difficult claim, this time by the deceased's unmarried partner. In *Lewis v Warner*⁶, the deceased's entire estate passed to her daughter and her partner of 20 years, Mr Warner, received nothing. Mr Warner (who was 91) wanted to remain living in the home he had shared with the deceased, in part because his neighbours cared for him. However, Mr Warner had signed a declaration that he would not make any claim for the house, accepted he had no "moral" claim to the home and was able to purchase alternative accommodation.

The deceased's daughter did not want Mr Warner to live in the house (even if he purchased it) and argued that Mr Warner did not need the house for his maintenance. The court disagreed and awarded Mr Warner an option to purchase the deceased's home for its market value. This

indicates both the breadth of the court's powers and the fact that the merits of an application can be finely balanced.

A safety net?

The ability to make a claim for reasonable financial provision can provide a useful safety net for those who are not adequately provided for following the death of a close friend or relative. However, it is clear that the success of an application is likely to depend on the facts and so thorough preparation is essential.

- An application for reasonable financial provision can be made either before a grant of probate or within six months after it has been issued. So taking legal advice as soon as possible is recommended.
- Evidence of any maintenance provided by the deceased, the relationship between the deceased and the potential applicant and the financial resources of the potential applicant and of any beneficiaries is important.
- Before embarking on court action applicants should normally try to resolve the claim by agreement with the executors. Court claims can be expensive; as with all litigation, success is not guaranteed and losing may mean a claimant has to pay the executors' legal costs as well as their own.

Notes

2. Inheritance (Provision for Family and Dependents) Act 1975
3. *Illott v The Blue Cross and others* [2017] UKSC 17
4. [2017] UKSC 17
5. *In re Jennings, deceased* [1994] Ch 286
6. [2017] EWCA 2182

RPC asks

Inheritance tax – is reform on the way?

Popular opinion has long regarded inheritance tax with some disdain, and this is compounded by the administrative burden imposed by the current regime. Although inheritance tax is payable in respect of fewer than 5% of all deaths returns must be submitted whether liability has accrued or not. The rules governing when particular reliefs from inheritance tax apply are complex and can be difficult to navigate.

In January 2018, the Chancellor asked the Office of Tax Simplification (OTS) to undertake a two-part review of inheritance tax, with a view to simplifying the current regime and make the customer experience as smooth as possible. The OTS ran a public consultation during the first half of 2018, and recently published the first of two reports.

The OTS review

The [first report](#) focussed on the issues and complexities raised during the consultation in relation to the administration of estates as well as other inheritance tax charges.

The key takeaway from the report was the need for the current system to be replaced by an automated, digital system. To achieve this, the report encouraged HMRC to review and improve the inheritance tax customer journey and made several recommendations.

- **Forms and guidance:** Very short forms should be introduced for the simplest estates and worked examples, case studies and an online inheritance tax calculator should be provided. Returns for assets for which no inheritance tax is due should be removed.
- **Payment:** The payment process should be overhauled, and an automated system for providing payment receipts should be introduced.
- **Probate:** HMRC should liaise with HM Courts and Tribunals Service to streamline the process for paying tax and obtaining probate.

The first report also revealed that high value estates are paying less tax than those with a lower value. With lower value estates predominately made up of residential property, the steady rise of property values has caused many unintentionally to accrue inheritance tax liability. As such, many estates may benefit from effective tax planning to restructure their estates.

What next?

The OTS is due to publish its second report during the spring. This report will consider areas of complexity within the inheritance tax rules, with recommendations for further reform likely. The first report indicates that the OTS had received a range of suggestions as to how the various reliefs could be simplified.

Proposed reform is also not limited to inheritance tax. Through HMRC, the Government is holding a [public consultation on the taxation of trusts](#). Whilst acknowledging that trusts are an integral part of the UK's legal system, the review sought to assess whether the current tax regime meets the desired principles of transparency, fairness and simplicity. The review closes on 28 February 2019, and any proposals which follow will be of interest to those who have, or are looking to, diversify their assets.

While tax reform is in the pipeline, the current regime is unlikely to be overhauled any time soon given the political focus elsewhere. Nevertheless, the OTS's first report highlighted the need for many estates to review whether they can restructure their estates to be more tax-efficient. Regardless of the current fluctuations in the property market, estate holders should review their current tax planning to ensure they are taking take advantage of the tax reliefs available.

And finally ...

The TerraLex asset tracing guide is here!

We have assembled and published the TerraLex Guide to Tracing Assets Around the World. The guide contains contributions from lawyers in the TerraLex network, which covers over 100 jurisdictions across a number of territories in the Americas, Europe and Asia.

RPC edited the guide which provides an overview of asset tracing in the United Kingdom. RPC's contribution considers: what information about assets is publicly available; what assets can be frozen; how assets can be protected on an interim basis; and how to obtain a search order or freezing injunction.

A copy of the guide can be found [here](#).

The RPC private wealth disputes team

Disputes can get complex. As one of the few top law firms handling private wealth litigation, our large team of lawyers has an impressive track record of handling disputes both in and out of court. We act for trustees, family offices and other asset and wealth holders and commonly act against HMRC. Drawing on extensive tax, asset management and commercial expertise, we can help resolve any type of dispute, from family settlements and inheritance issues to conflicts over assets, including art and valuables. We have a global reach with offices in London, Hong Kong and Singapore, and access to the TerraLex network of lawyers in over 100 jurisdictions.



Adam Craggs
Partner
+44 20 3060 6421
adam.craggs@rpc.co.uk

Area of expertise:
Tax disputes



Geraldine Elliott
Partner
+44 20 3060 6435
geraldine.elliott@rpc.co.uk

Area of expertise:
Private wealth and trusts disputes



Davina Given
Partner
+44 20 3060 6534
davina.given@rpc.co.uk

Area of expertise:
Art disputes



Emma West
Associate
+44 20 3060 6508
emma.west@rpc.co.uk

Area of expertise:
Private wealth and trusts disputes