

[2005 JLR 421]

IN THE MATTER OF THE R.E. SESEMANN WILL TRUST

ROYAL COURT (Birt, Deputy Bailiff and Jurats Le Brocq and Clapham): November 3rd, 2005

Trusts-rectification-discretion of court-may order rectification if (a) by genuine mistake, deed fails to carry out parties' intention; (b) full and frank disclosure; and (c) no other practical remedy-distinction between intention and objective-no rectification if deed carries out parties' intention but fails to achieve objective sought

The trustee of a settlement applied for rectification of a deed which excluded the settlor from benefiting under it.

The settlor, his children and grandchildren were beneficiaries under a trust which held shares in a company. The trustee had a power to add anyone except an excluded person as a beneficiary. It could also declare anyone, including a beneficiary, to be an excluded person, who could not benefit directly or indirectly from the trust. The settlor's wife was not a beneficiary or an excluded person.

A buy-back of shares by the company was proposed but under s.660A(1) of the Income and Corporation Taxes Act 1988 the settlor would have been liable to UK tax on the income arising under the trust because he had an interest in it. After obtaining legal advice as to how the settlor might avoid this liability, it was intended to exclude him absolutely from benefit under the trust. A deed of exclusion was therefore executed which declared the settlor to be an excluded person. The Inland Revenue claimed, however, that the settlor remained liable to tax on the income as his wife could have been added as a beneficiary and, under s.660A(2) of the 1988 Act, a settlor was deemed to have an interest in property which ". . . is, or will or may become, payable to or applicable for the benefit of the settlor or his spouse in any circumstances."

The trustee denied that it could have added the settlor's wife as a beneficiary if a benefit might thereby have been conferred on the settlor, as to do so would have breached the trust requirement that an excluded person should not receive any direct or indirect benefit from the trust. As an alternative, it brought the present proceedings seeking the rectification of the deed of exclusion by adding a provision specifically excluding the settlor's wife and any future wife from benefiting under the trust.

The trustee submitted that, whilst it had not been intended that the deed of exclusion should have excluded the settlor's wife, it should be rectified

2005 JLR 422

as it did not achieve the agreed objective, namely that the settlor should not be liable to UK tax on the income from the buy-back of shares.

Held, refusing to rectify the deed:

As the deed which declared the settlor to be an excluded person accurately reflected the trustee's intention to exclude him from benefiting under the trust, it would not be rectified. It had not also been intended to exclude the present and any future wife of the settlor. A document could be rectified if (a) there had been a genuine mistake, so that it did not carry out the parties'

intention; (b) there had been full and frank disclosure; and (c) there was no other practical remedy. There was, however, an important distinction between a document that failed to achieve the transaction the parties had intended, which could be rectified, and a document that merely failed to achieve their objective, which could not be rectified. Rectification would not be used to enable parties to enter into a transaction that, with hindsight, would have been more desirable than the one they had actually intended. The deed of exclusion would not, therefore, be rectified merely because it might not have achieved the desired objective that the settlor should not be liable to UK tax in respect of the trust income. The fact that the purpose of rectification would have been to enable the settlor to avoid paying UK tax was not in itself, however, a bar to the relief sought ([paras. 12–13](#); [paras. 18–20](#)).

Cases cited:

- (1) *Racal Group Servs. Ltd. v. Ashmore*, [1995] STC 1151, applied.
- (2) *Sherdley v. Sherdley*, [1986] 1 W.L.R. 732; [1986] 2 All E.R. 202, *dicta* of Donaldson, M.R. applied.

Legislation construed:

Income and Corporation Taxes Act 1988 (c.1), s.660A, as added by the Finance Act 1995 (c.4), s.74 and Schedule 17, Pt. 1:

- “(1) Income arising under a settlement during the life of the settlor shall be treated for all purposes of the Income Tax Acts as the income of the settlor ... unless the income arises from property in which the settlor has no interest.
- (2) . . . [A] settlor shall be regarded as having an interest in property if that property ... is, or will or may become, payable to or applicable for the benefit of the settlor or his spouse in any circumstances whatsoever.”

D. Cadin for the representor;

M. Renouf on behalf of *T. Hanson*, as representative of the interests of the beneficiaries and guardian *ad litem* of the minor beneficiaries.

1 **BIRT, DEPUTY BAILIFF:** This is an application for rectification of the R.E. Sesemann Will Trust. It is not straightforward.

2005 JLR 423

The factual background

2 The following facts appear from the evidence before us. R.E. Sesemann died on September 1st, 1990. By his will he bequeathed his shares in a certain company to his son Michael (“the settlor”). By a deed of variation dated March 16th, 1991 the will was varied so that the shares in the company were bequeathed to the representor (“the trustee”) upon the trusts set out in the schedule to the deed of variation. That trust is known as the R.E. Sesemann Will Trust and we shall refer to it as “the trust.” The trust is a conventional discretionary trust governed by Jersey law. The beneficiaries named in the deed were the settlor, his three children and any issue or dependants of the settlor or any of his children. There was power to add any person (other than an excluded person) as a beneficiary. There was also power to declare any beneficiary or other person to be an excluded

person. Under cl. 25 no excluded person was to be capable of taking any benefit of any kind directly or indirectly by virtue or in consequence of the trust. Under the law of the United Kingdom, the deed of variation had the effect of deeming the settlor as settlor of the trust for the purposes of UK income tax and capital gains tax.

3 In 1996/1997 it was proposed that the company should return cash to its shareholders through a buy-back of shares. A proportion of the proceeds would be treated as income for UK tax purposes. Although the settlor was a named beneficiary at the time the trust was created, he had by 1997 ceased to have any wish or expectation that he or his wife would benefit from the trust and he viewed the trust as one which was to be the primary source of financial security for his grandchildren. Furthermore, it was necessary for tax purposes for the settlor to cease to be able to benefit from the trust, as otherwise the income element of the buy-back proceeds would be treated as his income for UK purposes, regardless of whether or not he actually received a benefit.

4 The English adviser to the settlor and the trustee was Mr. Leslie John Powell, a solicitor with Richards Butler. The person dealing with matters at the Jersey end was Advocate Dart. Both have sworn affidavits and Advocate Dart has exhibited his attendance notes. Mr. Powell and Advocate Dart liaised over the proposed buy-back and the proposed exclusion of the settlor.

5 At about 4:00 p.m. on November 14th, 1997, Mr. Powell telephoned Advocate Dart requesting, *inter alia*, that a deed of exclusion be prepared. The relevant part of Mr. Dart's attendance note reads as follows: "Michael S is treated as settlor for tax purposes so needs to be excluded. Deadline for this is end of next week (21/11/97). Can we do a deed of exclusion? Yes."

2005 JLR 424

6 Mr. Powell telephoned again at approximately 4:40 p.m. that day to confirm that the settlor needed to be excluded. Advocate Dart's attendance note reads as follows: "LP confirms-Michael Sesemann to be absolutely excluded. Reason-disposal of shares would be treated as dividend for tax purposes (MS taxable on same)."

7 Advocate Dart prepared a deed of exclusion and sent this to Mr. Powell by fax on November 17th. Mr. Powell confirmed the same day that he was satisfied with the draft and that it could be engrossed and executed. The deed was executed by the trustee on November 18th, 1997 ("the 1997 deed"). By the deed, the settlor was removed as a beneficiary and was constituted an excluded person.

8 For unrelated reasons, a further deed of exclusion was executed on April 1st, 1999. This constituted as excluded persons all the children of the settlor and any dependant of them or of the settlor himself. Accordingly, the beneficiaries at the present time are the grandchildren and remoter issue of the settlor and their dependants.

The problem

9 Section 660A of the Income and Corporation Taxes Act 1988 provides that the income of a trust shall be deemed to be that of the settlor unless he has no interest in the trust fund. Section 660A(2) provides that a settlor shall be regarded as having an interest in trust property if it will or may become payable to or applicable for the benefit of the settlor or his spouse in any circumstances whatsoever.

10 A dispute has arisen between the Inland Revenue and the trustee as to whether the trust is caught by s.660A. The Inland Revenue argues that there is nothing to prevent the trustee adding the settlor's wife as a beneficiary of the trust. In those circumstances, she could benefit and the trust is therefore caught by s.660A. The trustee, on the other hand, argues that it could not validly exercise its power to add the settlor's wife as a beneficiary because to do so would or might confer an indirect benefit on the settlor, which would be in breach of the provisions of the trust which require that an excluded person should not be capable of receiving any direct or indirect benefit from the trust.

11 It is not for this court to resolve these different views. That will fall for decision by the English High Court in the event of the Inland Revenue seeking to assess the settlor to income tax and his disputing such assessment. However, as an alternative solution, the trustee has applied to this court for rectification of the 1997 deed by adding a provision which specifically constitutes the settlor's spouse and any future spouse of the settlor as excluded persons.

2005 JLR 425

The nature of rectification

12 The test for rectification in Jersey is well established. There are three requirements:

(i) The court must be satisfied by sufficient evidence that a genuine mistake has been made so that the document does not carry out the true intention of the party(ies).

(ii) There must be full and frank disclosure.

(iii) There should be no other practical remedy. The remedy of rectification remains a discretionary remedy.

13 The important aspect in this case is whether the first requirement is met. There is a clear distinction to be drawn between the transaction itself and the objective behind the transaction. The court can rectify a deed which does not reflect the transaction which the parties intended to achieve but the court cannot use rectification as a method of allowing the parties to achieve some other transaction which, in hindsight, would have been more desirable.

14 We were referred to two cases which we found of assistance. In *Racal Group Servs. Ltd. v. Ashmore* (1), the English Court of Appeal refused to rectify a deed of covenant. The relevant part of the headnote to the report in *Simon's Tax Cases* reads ([1995] STC at 1152):

“The court could not rectify a document merely on the ground that it failed to achieve the grantor's fiscal objective. The specific intention of the grantor as to how the objective was to be achieved had to be shown if the deed was to be rectified. There was a real doubt about the specific intention of RGSL's financial controller and the evidence did not establish with the requisite clarity what was his and hence RGSL's intention as to when the covenanted payments should be made. RGSL had failed to establish to the required standard that the covenant did not give effect to its intention.”

15 We would quote from two passages in the judgment of Peter Gibson, L.J. He said (*ibid.*, at 1154):

“Before I consider those two grounds, I would make some general observations on the doctrine of rectification. Equity has power to rectify a written instrument to make it accord

with the true intention of the maker of that instrument. As it is put in *Snell's Principles of Equity* (29th edn, 1990) p626: 'What is rectified is not a mistake in the transaction itself, but a mistake in the way in which that transaction has been expressed in writing.'"

Peter Gibson, L.J. quoted with approval (*ibid.*, at 1158) the following passage from the judgment of Vinelott, J. in the court below:

2005 JLR 426

"What clearly happened is that neither Mr Keeley, nor Mr Hornby, appreciated that the effect of this alteration would be that the payments would no longer be a valid charge on RGSL's income. It may be that if that consequence had been drawn to their attention they would have amended the draft by providing for the payments in and after 1989 to be made on 20 July. They might equally have amended the draft to provide for four payments on 1 April in each year up to and including 1 April 1992. It cannot be said with sufficient confidence which course they would have taken if they had directed their minds to the provisions of the Income and Corporation Taxes Act 1988. Although the court will rectify a document if satisfied that it does not give effect to an agreement or an arrangement between the parties, or to the intentions of a grantor or covenantor, notwithstanding that all concerned want the deeds rectified to secure a fiscal advantage, the court cannot rectify a document in the absence of evidence establishing those facts merely on the ground that the document has failed to achieve a desired fiscal objective."

Peter Gibson, L.J. went on to say (*ibid.*):

"Mr Ewart accepted that the court cannot rectify a document merely on the ground that it failed to achieve the grantor's fiscal objective. The specific intention of the grantor as to how the objective was to be achieved must be shown if the court is to order rectification."

16 A similar point was made by Donaldson, M.R. in *Sherdley v. Sherdley* (2) ([1986] 2 All E.R. at 207):

"It is also a fact that the courts have rectified deeds when satisfied that they did not give effect to the interests of the parties, notwithstanding that what had triggered a desire and need for rectification was a purely fiscal consideration (see *Re Slocock's Will Trusts* [1979] 1 All E.R. 358) and that the decision of this court in *Whiteside v. Whiteside* [1949] 2 All E.R. 913, [1950] Ch. 65 to refuse such rectification was not based on the fact that the objective was a tax saving, but on the fact that the basic requirements for the exercise of the jurisdiction to rectify were not present, in that the deed precisely reflected the original intentions of the parties, which, in the light of better advice, they now wish they had executed in different terms ..."

Application to the facts of this case

17 Mr. Cadin concedes, quite properly, that there is no evidence before the court that any of those involved (*i.e.* Mr. Dart, Mr. Powell or the

2005 JLR 427

settlor) intended specifically to exclude the settlor's wife under the 1997 deed. What Mr. Cadin submits is that, as stated in the second attendance note of Advocate Dart referred to above, the intention was to exclude the settlor absolutely; in the circumstances, this meant excluding him in such a way that he could not be liable to UK income tax in respect of the trust's income. He relied in support on a letter dated April 29th, 2005 from the settlor to the trustee in which the settlor said this:

“I can confirm that the matters set out in paras. 12, 13 and 15 of Leslie Powell's draft affidavit are true. My objective in having the trustee execute the 1997 deed of exclusion was to ensure that both in fact, and for the purposes of the Inland Revenue, I would cease to benefit from the trust in any way. Had I been advised in or about 1997 prior to the execution of the deed that the wording included within the deed of exclusion was insufficient to achieve this objective, I would have given instructions to Mr. Powell, and therefore to the trustee, to execute a wider deed of exclusion, including, if so advised, the wording set out at para. 4(a) and (b) of the representation.”

18 The court has on many occasions made it clear that, as in England, the fact that there is a fiscal motive behind an application for rectification is no bar to the granting of such an application. But it is important that rectification should not be pushed beyond its proper boundaries. As already stated, it is not a mechanism whereby the court can assist the parties to enter into the document which they wished they had, rather than the document which they actually intended.

19 In our judgment, whilst the objective of the execution of the 1997 deed was undoubtedly to achieve the result that the income of the trust fund could not be attributed to the settlor for UK tax purposes, the intended method of achieving this was to exclude the settlor absolutely from benefit. The deed did just that. It constituted the settlor an excluded person which meant that he could not benefit directly or indirectly in any way.

20 What has happened is that those advising the trustee failed to take account of that provision of s.660A which deems a settlor to have an interest if his spouse can benefit in any way. If the Inland Revenue is right in its contention (as to which we make no comment), the 1997 deed did not achieve its objective. But it did achieve the intention of the parties. It may well be the case that, if the trustee had been advised at the time that, as well as excluding the settlor, the deed had also to exclude the settlor's spouse, the trustee would have executed a deed in that form. But that is not what was advised and one cannot say therefore that it was the trustee's intention. The objective was to remove any possibility of the settlor being liable to UK tax in respect of the income of the trust fund,

2005 JLR 428

but the parties intended to achieve that by excluding the settlor from benefit. The document reflected accurately the trustee's intention and it cannot therefore be rectified now simply because, with the benefit of hindsight, the parties wish that a different document had been drawn up, namely, one which excluded the settlor's spouse as well as the settlor. For these reasons, we refuse this application for rectification.

Application dismissed.