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Obtaining Guernsey trust documents: HMRC's powers

This article explores the powers of Her Majesty's Revenue Commissioners ("HMRC") in the UK to obtain copies of documents relating to Guernsey trusts, in light of a recent UK decision.

In the case of *HMRC v Panos Parisis, Adrian Towland and Ian Harrison*¹, a First-Tier Tax Tribunal in the UK (the "Tribunal") a hearing took place on 9 February 2011. HMRC wanted to impose penalties on three respondents who were the settlors of three different Guernsey law trusts (we will refer to the respondents individually as "Settlor" and together as the "Settlors"). Two of the respondents were also beneficiaries (together with their various family members) of two of the trusts.

HMRC alleged that the Settlers had failed to comply with notices issued under section 20(1) of the Taxes Management Act 1970 ("Section 20"). The notices required the Settlers to produce documents in their "possession or power". HMRC argued that the Settlers had not done so. Readers should note that, although Section 20 has now been repealed, the case remains relevant because of the powers of HMRC under schedule 36 of the Finance Act 2008 (Powers to Obtain Information and Documents).

Background to the case

HMRC were investigating three trusts, the Ionia Trust, the Jasper Trust and the Caraudavian Trust (together, the "Trusts") which owned shares in a BVI company ("BVI Co") and which in turn owned some of the intellectual property of an international group of companies, including Path Group PLC. The Settlers had been involved in the sale of the Path companies to a team of directors via a management buy-out.

The case centred around documents which HMRC argued that the Settlers had not produced, namely:

- the trust deed for the Caraudavian Trust (the "C Trust");
- the letter of wishes of the C Trust (or equivalent);
- all other correspondence and documentation issued when the Trusts were set up;
- all correspondence which had been generated in the intervening period for the C Trust;
- the trust accounts for all years from set up of the Trusts;
- the trust bank statements (or client ledger accounts if no separate bank accounts were operated for the Trusts); and
- copies of all accounts drawn up by BVI Co since it was incorporated.

HMRC accepted that a number of documents were not in the "possession" of the Settlers but argued that the documents were nonetheless within their "power". In fact, the documents were in the possession of the trustee of the Trusts, Bourse Trust Company Limited (the "Trustee").

The Tribunal noted that in Guernsey the position regarding disclosure of trust documents is set out in statute (as explained below). As we shall also explain below, there was some variation between the trust deeds for the Trusts, in that one Trust did not exclude the statutory provisions on disclosure but the other two Trusts did.

However, it was agreed that the Trusts (Guernsey) Law, 2007 (the "Trusts Law") was the law which applied to the trusts, so the Tribunal went on to consider the relevant sections of the Trusts Law, and in particular sections 26 and 38, in more detail.

Relevant provisions of the Trusts Law

Section 26 imposes a qualified duty on a trustee to provide “full and accurate information as to the state and amount of the trust property” on receipt of a written request from beneficiaries (including named charities), settlors and “trust officials” (defined as persons “...exercising a function or holding an office in respect of the trust, other than settlor, trustee or enforcer”).

A trustee’s obligation can be modified, as Section 26 goes on to state that “...the terms of the trust (may) prohibit or restrict the provision of any [such] information”. However, where the terms of a trust prohibit or restrict the provision of any information, a trustee, beneficiary, trust official or settlor may apply to the Royal Court for an order authorising or requiring the provision of the information. The application must show that provision of the information is “necessary or expedient”: for the proper disposal of any case before the Court, for the protection of any beneficiaries’ interests or for the proper administration or enforcement of the trust (section 26(3)).

Also relevant is Section 38 of the Trusts Law which provides that, subject to the terms of the trust and to any order of the Royal Court, a trustee is not obliged to disclose any letter of wishes or other documents revealing the trustee’s deliberations. However, an application can be made for disclosure of such documents but the burden is on the applicant seeking disclosure to show that this is “necessary or expedient”: for the proper disposal of any case before the Court, for the protection of any beneficiaries’ interests or for the proper administration or enforcement of the trust (section 38(3)).

Tribunal’s interpretation of the Trusts Law

Where does this leave us if HMRC has sent out a notice to a settlor requesting him to provide documents? In particular, what of the circumstance of where the documents are not in the settlor’s possession but may be within his control?

The Tribunal held that section 26 of the Trusts Law only applied to one of the trusts, the C Trust, as it did not have any terms in its trust deed restricting or prohibiting the disclosure of information to the Settlor.

The Tribunal held that, where section 26 of the Trusts Law applies and the duty to provide information is not excluded by the terms of the trust, then the trustee would be obliged on the request of a settlor or beneficiary to disclose copies of the following:

- the trust accounts for all years from set up;
- the trust bank statements (or client ledger account); and
- the trust deed.

(Remember that section 26 only requires a trustee to provide “full and accurate information as to the state and amount of the trust property” and does not extend to disclosure of trust deeds (and any deeds/instrument which are supplemental thereto).)

The Tribunal went on to accept that section 26 did **not** require production of the following items:

- the letter of wishes of the C Trust (or equivalent);
- all other correspondence and documentation issued from when the Trusts were set up; and
- all correspondence which had been generated in the intervening period for the C Trust.

As we have noted, the Tribunal held that section 26 only applied to the one trust, the C Trust, as it did not have terms in its trust deed restricting or prohibiting the disclosure of information to the Settlor. The effect of this was that, if an application was made by the Settlor of that trust, the Trustee would be obliged to disclose copies of those three types of documents (the trust accounts, bank statements and trust deed).

In contrast, the Tribunal concluded that the Trustee was not obliged to disclose the letter of wishes of the C Trust. In relation to that document, the Settlor would have to apply to the Royal Court under section 38 for an order requiring disclosure and to satisfy the Royal Court that disclosure was necessary or expedient for one of the three reasons noted above.

The Tribunal also concluded that section 26 extended to include an obligation to disclose the accounts of BVI Co (its shares were owned by the three Trusts). The Tribunal reasoned that although BVI Co was now dissolved, the company had been an asset of the C Trust and a *“full account of the current value of the trust must take into account what happened to past assets.”*ⁱⁱⁱ

The position was different in relation to the other two Trusts, as their terms did have the effect of prohibiting or restricting the statutory entitlement to information set out in section 26(2). In respect of those two Trusts, the Settlers would have to apply to the Royal Court for an order authorising/requiring the provision of the documents. This led to consideration of whether or not that ability meant that a document was in their possession or power.

Document in ‘possession or power’

Section 20 (of the Taxes Management Act 1970) required the Settlers to produce documents in their *“possession or power”*. The documents were in the possession of the Trustee, but were they in the power of the Settlers?

In the 1980 case of *Lonrho* iii the House of Lords adopted a narrow meaning of *“power”* in the context of litigation discovery procedures. *“Power”* was held to mean a presently enforceable legal right to obtain documents from whoever actually holds the documents, without the need to obtain the consent of anyone else. The Tribunal distinguished *Lonrho* on the basis of its different facts and differences in the disclosure provisions in the Rules of the Supreme Court.

The Tribunal agreed that the test of legal *“power”* of the Settlers (within the meaning of *Lonrho*) was not met by the

ability to take legal action under section 26(2) or 38(3) to compel the Trustee to disclose the documentation. It accepted that such actions were not guaranteed to be successful. Therefore, if the meaning of ‘power’ in section 20 was to be tested by this concept of having a legal ability to compel disclosure of documents, HMRC would fail. Indeed, it was notable that in the case of two of the Trusts, if the Trustee had disclosed the documents requested it would have breached the terms of the trust deeds as well as sections 26 and 38 of the Trusts Law.

The Tribunal speculated that if the Settlers of those two trusts had made an application to the Royal Court for disclosure under section 26, such an action was likely to fail. It would have been difficult for them to prove to the Court that the reason they were making the application (i.e. at the behest of HMRC) satisfied the test of being *“necessary or expedient for one of the three reasons cited above (for the proper disposal of any matter before the Court, for the protection of the interests of any beneficiary, or for the proper administration or enforcement of the trust)”*.

However, although the documents were not within the legal power or control of the Settlers, the Tribunal concluded that the documents were in their ‘de facto power’ based on an analysis of the relationship between the Trustees and Settlers and what documents in reality the Trustees were likely to provide on a request by the Settlers. Having regard to this analysis, the Tribunal noted that, if a person can obtain documents by requesting them, without having to incur large expense, then they are within his ‘power’, even if the person who has possession of the documents has the legal right to refuse disclosure.

As a matter of fact, the Settlers had not in fact requested the documents from the Trustee so that the Trustee did not have the opportunity to refuse disclosure. Nonetheless, the Tribunal concluded that the documents were within the power of the Settlers on a de facto basis as they would have been provided to the Settlers, had a request been made to the Trustees. Due to the Settlers’ failure to request the documents, the Settlers were found liable to a penalty under Section 20 of the Taxes Management Act for not disclosing

the requested documents to HMRC. It is worth noting that, had the Settlers actually requested the documents from the Trustee and the Trustee then refused disclosure, the Settlers would not have been liable to a penalty.

Commentary on decision

In light of the effect of section 26 of the Trusts Law, most Guernsey trusts will either exclude or modify its application. However, this still leaves the door open for beneficiaries and others to make an application under section 26(2) to Court for an order authorising or requiring disclosure in appropriate circumstances. This preserves the Court's supervisory jurisdiction.

It is worth bearing in mind that the Tribunal did not hear evidence on Guernsey case law, no doubt because, so far as we are aware, there are currently no Guernsey authorities on the effect of sections 26 and 38 of the Trusts Law. As readers may be aware, sections 26 and 38 came into force on 17 March 2008 with the enactment of the Trusts Law which replaced the Trusts (Guernsey) Law, 1989 (as amended) (the "1989 Trusts Law"). Sections 26 and 38 were extensive modifications of their predecessors, sections 22 and 33 respectively of the 1989 Trusts Law.

While the judgement can be criticised for its analysis of the meaning of sections 26 and 38 of the Trusts Law, for tax purposes it highlights the risks of the puzzling Section 20 of the Taxes Management Act 1970 to settlors/beneficiaries who have been issued with an information notice by HMRC under this section. As noted above, the legacy of section 20 is found in paragraph 18 of part 4 of schedule 36 of the Finance Act 2008 (Powers to Obtain Information and Documents) which states that "(an HMRC) information notice only requires a person to produce a document if it is in the person's possession or power."

In concluding, we ponder whether this judgement leads to the analogy that, where documents are in a person's "power", this is tantamount to ownership? In the recent Privy Council decision in the Cayman Islands appeal of *Tasarruf Mevduati Sigorta Fonu v Merrill Lynch and Trust*

Company (Cayman) Limited and others^{iv} it was held that a settlor's power of revocation was in substance, if not in form, the equivalent of or tantamount to ownership under the laws of the Cayman Islands.

This Red Line is only intended to give a brief summary and general overview of this area of law. It is not intended to be, nor does it constitute, legal advice and should not be relied upon as doing so. If you would like legal advice or more information in relation to the matters covered in this Red Line or generally in relation to an fiduciary issue, please contact our fiduciary team on +44 (0)1481 723723, or by email at fiduciary@aohall.com. Members of our fiduciary team, together with their contact details, are listed on our website at www.aohall.com.

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ⁱ (TC01083) [2011] UKFTT 218 (TC)
ⁱⁱ *HMRC v Panos Parisis, Adrian Towland and Ian Harrison* (TC01083) [2011] UKFTT 218 (TC) at paragraph 40.
ⁱⁱⁱ *Lonrho Ltd & another v Shell Petroleum Co Ltd* [1980] 1 WLR 627
^{iv} [2011] UKPC 17

