

OLD SQUARE TAX CHAMBERS
SEMINAR JUNE 6th 2017 - VARIATIONS OF TRUSTS
SOME REASONS TO VARY TRUSTS
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Robert Venables Q.C.¹

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1. Variations under the Variation of Trusts Act 1958

1.1 How the Act Works

Court consents on behalf of those who cannot: minors, incapacitated, unascertained or unborn (“Non-Consenting Beneficiaries”)

Then general law comes into play, especially *Saunders v Vautier*

The Court cannot consent on behalf of ascertained persons of full age and capacity. They can thus prevent the variation.

The Court does not consent on behalf of HMRC!

1.2 Need for “Benefit”

1.2.1 The court cannot consent on behalf of a Non-Consenting Beneficiaries unless the variation is for their “benefit”.²

¹ Chairman of the Revenue Bar Association 2001-05, Bencher of the Middle Temple, Fellow of the Chartered Institute of Taxation, Chartered Tax Adviser, (Council Member 1999- 2011), TEP. Author of Non-Resident Trusts (9th edition forthcoming), The Taxation of Trusts 2010 (published by Key Haven June 2010, new edition with Oliver Marre entitled The Taxation of Trusts 2017 in preparation) The Taxation of Foundations (published by Key Haven 2010), Inheritance Tax Planning and numerous other works on trusts and tax. Senior Q.C. of Old Square Tax Chambers, Lincoln’s Inn.

² There is a very limited exception where the variation takes the form of lifting protective trusts.

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1.2.2 “Benefit” has two strands, financial and “moral”.

1.2.3 Court must be separately satisfied that the variation is for the benefit of each and every possible Non-Consenting Beneficiary.

This can be a real difficulty in many cases. See *In Re Cohen's Settlement Trusts, Eliot-Cohen v. Cohen and Others* [1965] 1 W.L.R. 1229 and the problem of disembodied souls.

In some recent cases, this principle has been overlooked.

1.2.4 Means of Ensuring that Variation will be for Benefit of Every Non-Consenting Beneficiary

1.2.4.1 HMRC The Loser

It is always helpful if there is a tax saving which means all the Non-Consenting Beneficiaries are better off.

1.2.4.2 Division of Trust Fund into Sub-Funds

A “carve up” of the Trust Fund into two or more Sub-Funds (which might include a Sub-Fund to which a beneficiary becomes absolutely entitled) may sometimes be appropriate. Each group of beneficiaries will take a larger interest in a smaller share.

1.2.4.3 Purchase of Insurance Policy

In some cases, it will be appropriate to purchase a single premium life-insurance policy to be held on trusts which will compensate those who would otherwise lose out from the variation but only if one or more beneficiaries did not attain a certain age. The terms of the insurance policy would mirror the trusts.

1.3 Residual Discretion of the Court

Even if the Court is satisfied the variation would be for the benefit of every person on whose behalf its consent is required, it does not have to approve the variation.

1.4 Preparing for a Variation

In many cases, preparing for the variation by varying the trusts otherwise than under the Variation of Trusts Act 1958 may be absolutely vital in ensuring the success of the application.

This can be done by exercise of powers of appointment or advancement, whether vested in trustees or individuals. The techniques are

- (a) to narrow down the number of beneficiaries and / or
- (b) to reduce the value of the interests of Non-Consenting Beneficiaries, ideally to a negligible amount.

1.5 Counsel Involved

1.5.1 General Comments

Counsel to be briefed will need to be chosen very carefully.

In any case involving tax considerations, they should be both tax and trusts specialists.

If the judge can rely on the integrity and industry of Counsel, he will grant the application that much more readily simply because he has confidence that Counsel will not “sell him a pup”.

1.5.2 Counsel Likely to be Needed

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Counsel for the Claimant

Counsel for the Trustees

Counsel for Minors (if any)

Counsel for Consenting Adults

2. Variations of Administrative Provisions Etc.

2.1 Extension of Purely Administrative Powers

Consider Trustee Act 1925 section 57 (rather than Variation of Trusts Act 1958) application if this is the only consideration.

2.2 Powers which are Partly Administrative and Partly Dispositive.

These are in effect variations of the beneficial interests and will need to pass the usual tests.

E.g. power to invest trust fund so as not to produce a reasonable income. Beware the effect of the Trusts (Capital and Income) Act 2013. In RV's view, this affects entitlements as between beneficiaries but does not remove liability for breach of trust.

E.g. powers to make loans to beneficiaries or to permit them to have the use of trust property on non-commercial terms

2.3 Powers, Indemnities and Exonerations which Affect the Trustees Personally

These will be looked at particularly carefully by the Court as the trustees are biased.

E.g. trustee remuneration, indemnity and exoneration.

They must be in the best interests of the beneficiaries. Can sometimes justify on grounds no suitable persons can be found to act as trustees. Have done this with very large trust funds where involved which needed professional trustees but no trustee could get sufficient indemnity insurance.

2.4 Other Powers

E.g. power to emigrate, powers of appointment and dismissal of trustees, provision for a Protector - especially if trust to be non-UK resident.

3. Variations Prolonging the Life of the Trust

Provided all the beneficiaries agree the perpetuity period and accumulation periods can be set running afresh - 125 years for each.

Very important to ascertain affect this will have on the interest of Non-Consenting Beneficiaries. Prima facie, they will not be benefited.

The tax advantages could be considerable and may well be enormous.

4. Protecting Beneficiaries Against Themselves

4.1 Lifting of Protective Trusts

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4.2 Creation of Protective Trusts and / or Postponing Age of Vesting

In the case of reprobates, the Court will be more sympathetic to moral benefit arguments and will look less to financial benefit.

5 Some Variations of Fixed-Interest Trusts

5.1 Terminating recognised interest in possession during lifetime of beneficiary

E.g. property held on trust for testator's widow for life, remainder to such of their children as survive widow her with substitutional gifts for their children if they do not and cross-acruers.

Division between widow and remaindermen to reduce overall charge to tax on termination of interest in possession. Widow makes potentially exempt transfer of value or chargeable transfer of value but hopefully at lower rate than on death.

Two Options:

(1) Share of remaindermen can be held in trust until (at least) the death of the widow - may not be desirable.

(2) Insurance Policy can be taken out in case children predecease widow and held on trust for issue of the child. The rest of the trust fund can be distributed.

5.2 Insertion of short-tem or revocable interests in income expectant on death of life tenant for the benefit of his surviving spouse.

This will work only where the interest of spouse will be recognised interest in possession when it falls into possession.

Aim is to avoid charge to inheritance tax on the death of the present Life Tenant and to replace it with either potentially exempt transfer of value or chargeable transfer of value when interest of his widow terminates.

6 Discretionary Trusts

Reducing the Class of Discretionary Beneficiaries

Increasing the Class of Discretionary Beneficiaries

7 Inheritance Tax Act 1984 section 142 Variations of the Estate of a Deceased Person

7.1 General Comment

7.2 Typical case

Property left to non-exempt beneficiaries, absolutely or on trust. Inserting of shortish interest in possession for surviving spouse so as

- (a) to convert chargeable transfer of value into potentially exempt transfer of value or

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(b) to convert chargeable transfer of value on death into lifetime chargeable transfer of value in each case to reduce charge to inheritance tax on the first death.

7.3 Drafting to Ensure that the Requirements of the Section are Met