

STEP JOURNAL

Downloaded on 15th July 2024 - 08:55

A matter of principle

A discussion on whether decisions of trust company directors are amenable to the Hastings-Bass principle.

In a recent case (*Re Wang Trust*, 12 April 2010, unreported) before the Grand Court of the Cayman Islands (Chief Justice Anthony Smellie QC), there fell for decision the application of the Hastings-Bass principle to an unusual situation: a Taiwanese individual migrating to Canada, established, on professional legal and accounting advice, a Canadian immigration trust structure, which, if established and operated correctly, will result in a five year Canadian tax holiday for foreign source (that is, non-Canadian) income from the time the immigrant becomes resident in Canada. Such a structure, which is well known and fully compliant with Canadian tax laws, involves the setting up of a foreign (that is, non-Canadian) trust, which owns and controls a foreign company; dividends declared by this company in favour of the trust during the five-year tax holiday, will not attract liability to Canadian tax. In the *Wang* case, the only dividend declared by the company in favour of the trust was declared after the expiry of the five-year tax holiday, as the result of a misapprehension as to the start date of the five-year period. Subsequent to the declaration and payment of the dividend, the Canadian Revenue Agency determined that the residence of the migrant (and settlor of the trust) in Canada had commenced some months before the date as understood by those advising the settlor when establishing the trust structure.

Had the company, instead of declaring a dividend, albeit outside the five-year tax holiday, made the payment to the trust as a distribution in the course of the winding up of the company, there would still have been a significant tax saving. In procuring the declaring of the dividend, instead of the making of a payment as a distribution in the winding up of the company, the trustee again acted on professional advice, which was, again, incorrect, in that had it been appreciated that the five-year tax holiday had already expired, the advice would have been that the company should make the payment by way of distribution in the winding up of the company, so as to obtain the more limited tax benefit applicable in those circumstances.

The settlor of the trust (which was governed by Cayman Islands law) brought a Hastings-Bass application in the Cayman Islands Courts, seeking a declaration that the decision of the trustee (a Cayman corporate entity) to procure the dividend to be declared in its favour by the company, and also the receipt of the money by the trustee as a dividend, were void; the settlor also sought a declaration against the directors of the company, and the company itself, that the resolution to declare the dividend, and the payment of the dividend by the company itself, were also respectively void on the Hastings-Bass principle. The principle is recognised and applied in the Cayman Islands: *Barclays Private Bank & Trust (Cayman) Ltd v Chamberlain*, 2004 (unreported), and *A v Rothschild Trust Cayman Limited* [2004-5] CILR 485. The case for the settlor was put in two ways; the actions of the trustee were plainly void on the Hastings-Bass principle. In deciding to procure the payment of the dividend and to receive it based on the erroneous advice that it had received, the trustee took into account the wrong date as the expiry of the five-year tax holiday – a decision that it would not have taken had it been aware of the true expiry date. That decision was taken in error, with detrimental tax consequences for the trust, and, in consequence, the decision was liable to be set aside, on the Hastings-Bass principle, as being a decision it had no authority to make, because it was a decision that

could not have the intended beneficial consequences for the trust. As regards the actions of the directors and the company, which took place at the instance of the trustee, the case for the settlor was, primarily, that the substance of the entire transaction under which the dividend was declared and paid to the trust, was the act of the trustee itself, acting through its nominee directors of the trust company, and accordingly all the elements in the payment of the dividend were void on the Hastings-Bass principle as applied to the acts of the trustee. If that was wrong, then the acts of the directors themselves, and accordingly those of the company, were themselves amenable to the Hastings-Bass principle, as the directors were fiduciaries for their company, and the sole purpose of the establishment and object of the company was to achieve the intended tax benefit, which in the event had failed, through error on the part of the directors.

The Grand Court had no difficulty in concluding that the actions of the trustee, in procuring the payment of the dividend to itself, and the receipt by the trustee of the dividend, were void. The Court was also prepared to hold, following the first instance English High Court decisions of *Hunter v Sennett Support Services* [2004] EWHC 1085, and *Pitt & Anor v Holt and the Commissioners of Her Majesty's Revenue & Customs* [2010] EWHC 45, that the acts of the directors were themselves amenable to the Hastings-Bass principle. There was, however, no evidence as to the state of mind of the directors when resolving to declare the dividend – the transaction had taken place some years earlier, and no evidence was available. The Court was not persuaded by the argument that it could be safely assumed that the directors either acted on the same misapprehension as the trustee as to the relevant date by which the dividend had to be declared in order to achieve the intended tax consequences, or they failed to have regard to it at all, so that in either case the Hastings-Bass principle applied to their decision. The Court accordingly held that it was unable to declare void the acts of the directors or the company, without evidence as to the state of mind of the directors when considering the resolution to declare the dividend. With regard to the argument that the entire transaction was, as a matter of substance, to be regarded as the acts of the trustee, the Court was unimpressed, and held that it would be a contradiction in terms to hold that the decisions of directors who are mere nominees and merely acting on the directions of their principal, can be set aside on the Hastings-Bass principle, which requires that the decision in question is that of the fiduciary decision maker and of no-one else.

The case for the settlor was carefully put on the basis that the application of the Hastings-Bass principle to the acts of the directors and the company in the circumstances, was merely an application of the established Hastings-Bass principle to an unusual set of facts, and was not an extension of the principle itself – in the current climate, any suggestion of an extension of the principle could be expected to fall on somewhat stony ground. It remains to be seen whether, and if so to what extent, the Hastings-Bass principle survives its apparent growing unpopularity as a concept, and attacks such as those mounted in *Pitt and Re Futter (No. 3) Life Interest Settlement* [2010] EWHC 449 (Ch).

<https://journal.step.org/step-journal-july-aug-2010/matter-principle>