RISK ASSURED
LIFE INSURANCE SPECIALISTS

Consequences of a wrong appointment from a pre-22 March 2006 flexible trust

Synopsis: In Hopes v Burton [2022] EWHC 2770 (Ch) the Court agreed to set aside two deeds of appointment thus saving the trustees a potential tax liability of over £400,000.

Date published: 05.12.2022

Court cases involving life policy trusts are not that common, and since the best learning method is to learn from (preferably someone else's) mistakes, this recent decision is most welcome.

The case concerned two deeds of appointment made in 2013 and in 2014 by the trustees of a trust ("the trust") made by Hilary Marsden (formerly known as Hilary Burton – "the settlor") in 1992 in respect of a policy held by her with Skandia Life.

The trust in question was a "typical" trust offered by life offices until 2006: a flexible power of appointment interest in possession trust, with Box A "Possible Beneficiaries" and Box B "Immediate Beneficiaries". Four Immediate Beneficiaries were named.

The settlor appointed her then accountant and solicitor as additional trustees. The settlor died in 2004, but it was only in 2012 that the Skandia policy came to light. The value of the policy was then £2.15 million. The original trustees agreed to step down and new ones were appointed.

In 2013, the new trustees met with a solicitor to discuss the trust and a deed of appointment was drafted in favour of several beneficiaries. The intention was to keep some of the beneficiaries' interests intact, remove one of the immediate beneficiaries and create a discretionary trust in respect of another part of the trust fund. It was apparently understood that the appointment of one share would create a discretionary trust and would have inheritance tax (IHT) consequences, the tax to be paid from that share. In 2014, another deed of appointment was executed to appoint one part of the trust fund also on discretionary trust.

In 2017, the trustees took advice from specialist tax counsel, Emma Chamberlain. Her advice in summary was that...

(1) the 2013 appointment did not leave the interests of the three existing beneficiaries as they were (as had been intended), but instead revoked the previously qualifying interests in possession for all four funds, and, HMRC were likely to argue, created new non-qualifying interests in possession; and

(2) because both the appointments were revocable, the Immediate Beneficiaries retained the possibility of benefitting from the trust fund in the future, and the appointments were likely to be treated as gifts with reservation of benefit.

As to the amount of tax payable in consequence of the appointments, the trustees were advised that there was an immediate charge of £365,000, plus interest of

over £68,000. In addition, ten-yearly IHT charges would apply and appointments out of the trust fund would be subject to exit charges.

The application (claim) to set aside the two *"offending"* deeds was made by the trustees in 2021. The main ground was that the trustees made an operative mistake as to the substance or effect of the deeds. In particular, the 2013 appointment was said to have mistakenly (and unnecessarily) included provisions which terminated existing interests in possession and appointed new ones in their place, when there was no intention to do so.

After considering the evidence, in particular the subsequent actions of the trustees (who made capital distributions which they could make under the original trust but not under the deed of appointment) and the relevant case law, the judge decided that the 2013 appointment indeed created radically different interests held by the immediate beneficiaries, and that the trustees were mistaken in doing so.

This mistaken belief was in his judgment *"sufficiently serious as to make it unconscionable not to set aside both appointments".*

Comment

This case perfectly illustrates the dangers of making changes to beneficiaries under pre-22 March 2006 flexible interest in possession trusts.

Even the involvement of solicitors does not necessarily save you from getting it wrong (compounded in this case by different members of the firm dealing with different aspects of the case and clearly not communicating sufficiently well). Thankfully, the trustees in this case managed to avoid the eye watering tax bill, but bringing such an application to Court must have cost a substantial sum as well.

Remember that in the case of a mistake, there are two possibilities of a remedy – either to rectify the deed or to rescind (set aside) the transaction. In both cases, a Court application will be needed. Obviously, the Court will examine any evidence and decide on the facts of the case. But nothing is ever guaranteed, so it is best not to get it wrong in the first place.