

Revisiting the principles of equitable mistake

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In a recent decision, the Royal Court of Guernsey considered whether to set aside a distribution on the grounds of equitable mistake where that mistake led to adverse UK tax consequences. This is the first time that the principles of equitable mistake have been considered in Guernsey since the seminal decision of the UK Supreme Court in *Pitt v Holt* [2013] UKSC 26.

The facts of *Gresh v RBC Trust Company* (unreported) can be summarised as follows. Mr Gresh was a member of a pension plan administered by a Guernsey trustee. He had been advised by independent tax advisers that any lump sum distribution made to him would be tax free provided that the distribution was not remitted to him in the UK. When he turned 50, Mr Gresh requested a lump sum distribution from the trustee of his pension fund.

The trustee believed the advice to be accurate and gave instructions for the requested transfers to be made. The advice was wrong in that only periodic payments would be tax free even if any capital sum was retained outside the UK. The distribution made to Mr Gresh has been assessed in the UK to a tax liability of 40 per cent, leaving Mr Gresh facing a very significant tax bill.

Mr Gresh's application, originally before the court in 2010, requested the setting aside of the distribution on *Hastings-Bass* principles, but following the Supreme Court decision in *Pitt* the application was amended and proceeded upon the grounds of equitable mistake. HMRC was latterly joined to the application and opposed it while the trustee remained neutral.

Test for equitable mistake

The Bailiff considered that *Pitt* was highly persuasive in Guernsey and that he was not aware of any reason why the principles set out by Lord Walker in *Pitt* should not be applied. The main issues for consideration were:

- What was the legal test set out by *Pitt*? Was it that the mistake should be of sufficient gravity to justify it being set aside on the ground that it would be unconscionable or unjust to leave it uncorrected? Alternatively, was the test that the mistake was sufficiently serious for it to be unconscionable for the donee to retain the property given to him?

- What is the meaning of 'unconscionability' (unjust or unfair) in these circumstances?

The Bailiff ruled that the decision in Pitt had not altered the test for equitable mistake. It was still a requirement to look at all the relevant circumstances of the mistake and the consequences for the person who made the transfer in question, in order to evaluate objectively the injustice of leaving the disposition uncorrected.

Not unjust or unconscionable

Applying these principles, the Bailiff found that it would not be an appropriate exercise of the court's jurisdiction to set aside the disposition. While it was clear that Mr Gresh (and the trustee) believed and relied upon advice which turned out to be incorrect, he was not seeking to pursue an aggressive tax avoidance scheme. As such, it was not unconscionable for Mr Gresh to retain the proceeds of the distribution made by the trustee for the following reasons:

- In Pitt, a significant element in the Supreme Court's analysis was that if the mistake had not been corrected, there would have been insufficient funds in the settlement available to provide for Mr Pitt in circumstances where the settlement had only been created in order to provide for his care following serious injuries suffered in an accident.
- The only person affected in this case was Mr Gresh, who would have a large tax liability if the mistake was not corrected.
- Mr Gresh had a contractual relationship with the tax advisers who had provided the incorrect advice. Therefore, it could be distinguished from cases where it has been found unjust to require settlors or beneficiaries to bring litigation against former professional advisers.

The clear guidance from the Royal Court that not every mistake as to tax consequences based on incorrect or negligent professional advice will be corrected by the courts is noteworthy. While the court was not in a position to form a view as to whether Mr Gresh may have an action against his tax advisers, this was a reminder that there are occasions when it is more appropriate for professional indemnity insurers to pick up the pieces rather than the courts.

The Royal Court also demonstrated that in considering the requirement that it would be unjust or unconscionable to leave the mistake uncorrected, it is not concerned with whether the donor was engaged in tax avoidance, which neither Mr Gresh nor the trustee were in this case. The crucial element was the effect of the transfer which meant that Mr Gresh retained the benefit of the distribution.

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