A NOTE ON LEON SARTIN'S TAX RECOVERY CLAIMS BY THE SETTLOR

Robert Venables QC[1]

This is an extremely difficult area, where it is impossible to be dogmatic. I would myself respectfully differ from Mr Sartin's statement: "The tax liability is, of course, that of the UK settlor not the offshore trustees. The settlor is not a nominee of the UK government." I append to this note an extract from my *Non-Resident Trusts* at 13.10.4, in the context of the discussion of double taxation treaty relief.

I note that if the indemnity is enforceable abroad, it would be an easy matter for the UK Parliament to impose on any third party a liability which it could *de facto* enforce, and to give that third party a right of indemnity against a person outside its jurisdiction it in fact wanted to but could not tax. Is a matter of public policy to come down in 1999 to a question of form rather than substance?

Venables on Non-Resident Trusts 7th Edition

13.10.4 Double Taxation Relief of Trustees[2]

Suppose that the trustees are residents of Contracting State B for the purposes of a double taxation arrangement between that State and the UK. Under the double taxation arrangement they are exempted from UK capital gains tax in respect of all the gains they have actually realised during the year of assessment. The settlor himself cannot rely directly on the double taxation arrangement. In my view, there is a very respectable argument that the settlor can rely indirectly on the double taxation arrangement.

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2 The argument in this section is independent of, and rather stronger than, that mentioned in 13.7.1.3.3.

Looking at the matter, as modern courts like to do, as one of substance rather than form, it is quite clear that the Schedule levies capital gains tax on the trustees and not the settlor. True, the measure of the capital gains tax payable is determined by reference to the settlor's personal tax circumstances. True also, that in the first instance it is the settlor who is liable to pay the tax to the exclusion of the trustees who cannot be assessed directly. Yet at the end of the day, provided the machinery of the Schedule works properly, it is the trustees who will pay the tax. It is thus in substance borne by them and the whole of the Schedule is mere machinery used to calculate the rate of tax and facilitate its collection by the Revenue. Viewed in this light, is it not clear that the double taxation arrangement, and the relevant enabling UK legislation, effectively prevent tax being recovered from the trustees in such a case? Is it therefore not equally clear that the settlor cannot be made liable in the first place, as his liability would be transformed from a mere representative and secondary liability into an entirely new primary and definitive liability?

Put the argument another way. Suppose that the settlor is assessed under the section, pays the tax and recovers it from the trustees. What is to prevent the trustees making a claim for relief and for repayment of the tax under the double taxation arrangement?

If this argument is correct, it is crucial that the gain should actually be relieved from UK capital gains tax under the terms of the double taxation arrangement. It is not enough that, the Schedule apart, the trustees would not be liable, simply because they did not satisfy the residence test laid down in Taxation of Chargeable Gains Act 1992 section 2(1). The precise wording of the relevant double taxation arrangement will be crucial.[3]

3 See my *Capital Gains Tax Planning for Non-UK Residents*, Chapter 5.