Jersey shoots itself in the foot.

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Jersey's new trust laws have been the subject to some comment on this site, and in the Jersey and UK national press, at least partly as a result. There is, however, more to say. Whilst considering the emails that were sent to the Observer two weeks ago it occurred to me that the consequences of Jersey's new trust laws are much more significant than the fact that they simply legitimise tax evasion of a type which has, according to Jersey officials, been going on anyway.

What they also do is fundamentally undermine the status of the Jersey trust. They do this for one simple reason. Every single Jersey trust can now be revoked, whatever the trust deed says. The power to revoke is included in the new trust law passed by the States of Jersey in April 2006, and even if a trust was originally written saying that revocation was not allowed Jersey law now allows that trust to be amended so that revocation will be possible in the future. And since it is the policy of Jersey to encourage this, and since the Courts of Jersey are now only allowed to consider Jersey law in deciding whether this should happen or not, and that law says it should be allowed, then it is not difficult to see that my argument is based both on law and on the current stated wishes of the Jersey political elite, as reflected in the emails published two weeks ago.

What is important are the ramifications of this. They may be fairly serious for the Jersey finance industry. The reason is simple. For a trust to be recognised as tax effective in English law (which is the recognised basis of most trust law around the world and which is, therefore the model with which trusts usually have to comply to be acceptable for tax planning) the settlor of a trust (i.e. the person who creates it) has to make an irrevocable statement that they will never benefit from the asset he or she has gifted into trust again. If they cannot do that, or of the law of the territory where the trust is created allows them to change their mind (as Jersey now does) then instead of the settlor being treated as having given the assets away so that they are no longer taxed on the income and gains arising from the trust assets they are instead treated as if they still owned them and as such it is presumed that the trust does not exist for tax purposes in the UK, and no doubt in many other places as well.

Jersey has abandoned English trust law as the basis of its own trust law by passing its new trust laws in 2006. As a result the UK should now consider any trust in Jersey to be a 'bare trust'. This sort of trust is defined as follows:

> A bare trust (sometimes referred to as a simple trust) is one in which the beneficiary has a right to both income and capital and may call for both to be remitted into their own name, they are also entitled to take actual ownership and control of the trust property. Although there are trustees, they are only effectively nominees and must act according to the beneficiary's instructions.

And this is exactly what Jersey has created as the only type of trust now available in Jersey by ensuring that all trusts are revocable and that all the powers of management of the trust can be effectively retained by the settlor. If evidence is needed Paul de Gruchy, who according to Senator Walker was responsible for steering the new trust laws through the States, provided it when he wrote on 14 September that:

> Currently, it is common for assets such as shares in a family company to be placed in trust, but for the settlor to wish to retain control over how the company is operated. Or an investment portfolio may be placed in trust, but the settlor may wish to manage the investments.

But he then noted that if as a result:

> the discretion of the trustee is fettered, there is a risk that the trust could subsequently be attacked as a sham. For an international client, these are reasons to not use a Jersey trust.

So the new law were explicitly designed to overcome this by allowing the settlor to do what they like. This might have resolved a problem in Jersey law, where the published email correspondence suggests that such sham trusts were commonplace, whatever the law might have said to date, but it does not change the law elsewhere. As a result:

Jersey trusts should no longer be considered as such in the UK and other countries with trust legislation similar to that in the UK. They are instead bare trusts, meaning that all tax planning, past, present and future relying on Jersey trusts being irrevocable is likely to now have failed in the UK and elsewhere, whatever has been the case to date. If the settlor of the trust is now alive it is likely that they should be taxed on all the trust's income and gains.

Because Jersey trusts are now mere nominee arrangements or bare trusts the EU Savings Tax Directive exemption for trusts is no longer available for any Jersey trust with an EU resident settlor and all the relevant income of such trusts is now subject to the provisions of that directive and will either have to be disclosed in the country in which the settlor now resides or be subject to tax withholding in Jersey;

The Jersey corporate 'Special Purpose Vehicle' market has depended upon the irrevocable nature of Jersey trusts. Since all Jersey trusts can now be revoked these Special Purpose Vehicles are no longer independent of the companies that promoted them and as such it seems that the debt that SPVs have securitised will now have to be shown on the balance sheets of their sponsoring companies, the precise outcome they sought to avoid.

In effect Jersey has shot itself in the foot with its new trust laws. By regularising what was known to be a sham Jersey has ensured that all Jersey trusts should instead now be considered shams elsewhere. The consequences for Jersey cannot be understated. But for once it has only itself to blame.

My full report setting out my reasoning in support of these conclusions is available here.

Richard Murphy.