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Prepare for lift-off

As the implementation date of the EU Succession Regulation draws near, practitioners should get ready for a bumpy ride

The final countdown has begun to the implementation of *Regulation (EU) No.650/2012* (the Succession Regulation), which will have a significant impact on estate planning. As Richard Frimston TEP, Chair of the STEP EU Committee, observes: 'Although the UK, Denmark and Ireland are not bound by the Succession Regulation, it is ironic that it is likely to have a bigger effect in the UK than in many other EU member states. For some EU member states, the Succession Regulation does not introduce huge changes. However, a very large proportion of UK residents have connections and property in other parts of the EU, so that the regulation, on coming into full effect on 17 August 2015, will produce widespread changes for them. Practitioners need to be ready.'

In this edition, Sangna Chauhan considers the likely effect of the Succession Regulation on estate planning for internationally mobile families, and the importance of clients making an informed choice about the law that will govern succession to their estate.

Maria Grazia Antoci and Daniele Muritano similarly consider the effect that the Succession Regulation will have in Italy. They also share some other Italian perspectives on succession planning.

The European theme continues with an analysis by Susanne Thonemann-Micker and Jan-Lukas Lüken of how a deed of variation executed in accordance with the laws of England and Wales may be regarded from the perspective of German succession law.

There is another significant date approaching, although many practitioners will not be aware of it: the 150th anniversary of the death of John Banks falls on 28 July 2015. John Banks was the protagonist in the case of *Banks* v *Goodfellow*, in which Cockburn CJ provided the classic exposition of the requirements of testamentary capacity in England and Wales. Martyn Frost, Stephen Lawson and Robin Jacoby mark the occasion by unearthing the family story behind the case.

James J Holman, in his article 'Commercial realities', considers the use of trust structures in commercial transactions in the US, and the difficulties that can arise where hybrid vehicles combine both trust and corporate-law components.

We conclude this issue with a review by Andrew Kidd of a book by Grant M Jones and Peter Pexton, *ADR and Trusts*, which breaks new ground by providing an authoritative exploration of the law and the practice of arbitration and mediation of trust disputes.

We hope you enjoy this issue.

THE EDITORS

Crunch time

Clients should already be considering their choice of applicable law under the EU Succession Regulation. What are the factors to take into account?

By Sangna Chauhan

Abstract

- ***Regulation (EU) No. 650/2012*** **(the Succession Regulation) will apply from 17 August 2015.**
- **The Succession Regulation will have to coexist with extant treaties on succession law. Precedence is only taken by the Succession Regulation if those treaties have been concluded exclusively between member states.**
- **The Succession Regulation can affect individuals' estates if they have any connection to any of the member states in which the regulation has direct application. This includes individuals resident in the UK, Ireland, Denmark or resident outside the EU.**
- **Although the Succession Regulation broadly assists in simplifying cross-border estate planning, notable areas of uncertainty remain.**
- **A standardised approach in advising on the application of the Succession Regulation will be risky: the benefits of retaining existing planning must be balanced against those of making elections for the law of nationality to apply.**

'In order to allow citizens to avail themselves, with all legal certainty, of the benefits offered by the internal market, this Regulation should enable them to know in advance which law will apply to their succession.'

Recital 37 of *Regulation (EU) No.650/2012* (referred to throughout this article as the Succession Regulation) neatly summarises the intended objective behind the applicable law provisions at Chapter III of the Succession Regulation. But, as 17 August 2015 draws closer, has this objective of certainty been achieved?[1]

ESTATE PLANNING FOR INTERNATIONALLY MOBILE FAMILIES

On 17 August 2015, there will be a significant shift in international estate planning: the long-established (but often confusing, convoluted and contrary) private international law rules that apply on death will be affected, together with their practical consequences.

Although the Succession Regulation only substantially applies from later this year, it has been in force for almost three years. This should have been plenty of time for the regulation to have been properly scrutinised and guidance to have been issued to assist in clarifying the various issues that are inevitable with such a wide-ranging regulation.

1. References throughout this article to recitals and articles refer to the recitals and articles of the Succession Regulation

However, although there has been much analysis of the Succession Regulation, there is still a long way to go before its practical effects are uniformly understood across the EU.

The focus of this article is on how the Succession Regulation works and identifying some of its complexities. However, anyone waiting for an early answer to any of these unresolved questions is likely to be disappointed: it may take many years before the Court of Justice of the European Union (CJEU) is obliged to provide clarity in any of these areas.

IDENTIFYING THE 'FREE ESTATE'

The Succession Regulation clearly only applies to assets that constitute the 'free estate' of the deceased. Article 1(2) sets out a comprehensive list of what is excluded from the scope of the Succession Regulation. Paragraph (j) specifically excludes trusts, which is understandable given that, absent a testamentary power of appointment, assets held in trust do not usually form part of an estate.

Also, paragraph (g) refers to '... assets created or transferred... by way of gifts and joint ownership with a right of survivorship...'. This makes sense: under English and Welsh law, for example, a perfected gift is no longer in the estate and assets that are held as joint tenants pass by survivorship and not in accordance with a will or any relevant rules of intestacy. (Note, however, that paragraph (i) of article 23(2) Succession Regulation preserves the obligation to 'account for gifts, advancements or legacies when determining the shares of different beneficiaries'. This potential 'clawback' of lifetime gifts is one of the key reasons that the UK chose not to adopt the Succession Regulation.)

Likewise, the effects of matrimonial property regimes are excluded from the scope of the Succession Regulation (paragraph (d) of article 1(2)). Historically, matrimonial property regimes have often been overlooked by lawyers in most common-law jurisdictions.[2] However, as families become increasingly mobile and international, to do so is perilous. Local law advice is often required to determine the exact effect of any matrimonial property regime that does apply (bearing in mind that not all matrimonial property regimes are identical).

2. The most obvious exception being some of the US states, which have community property matrimonial property regimes

UNDERSTANDING THE DIFFERENCE BETWEEN ESSENTIAL AND FORMAL VALIDITY

Although the Succession Regulation is a major change, it is by no means the only international convention in existence on succession or the disposition of assets on death.[3] Article 75 specifies that the Succession Regulation 'shall not affect the application of international conventions to which one or more Member States are party', though it then goes onto clarify that the Succession Regulation does take precedence over any such conventions that have been concluded exclusively between member states.

In this context, it is worth considering the *Hague Convention of 5 October 1961 on the Conflicts of Laws Relating to the Form of Testamentary Dispositions* (referred to here as the Hague Convention), which is specifically referred to in article 75. The Hague Convention is primarily aimed at harmonising the rules of formal validity and, as it has been ratified by a mix of 40 EU and non-EU states, it takes precedence over the Succession Regulation. Some EU states (e.g. Italy and Poland) are not subject to the Hague Convention and so, for them, the Succession Regulation must apply.

Although the Succession Regulation briefly touches upon the formal validity of dispositions on death, recital 52 specifies that any such rules must be 'consistent with those of the Hague Convention'. This is in accordance with the precedence given to the Hague Convention in article 75(1). The Succession Regulation achieves this by substantially reproducing the wording of the Hague Convention. In fact, the Succession Regulation goes further than the Hague Convention: in addition to dispositions on death, the Succession Regulation refers also to the formalities required for succession agreements. It is difficult to envisage how this increased scope might make the Succession Regulation incompatible with the Hague Convention.

3. Refer to Richard Frimston's article 'Tangled up in treaties' in the October 2014 edition of the *STEP Journal* for a starting point as to pre-existing succession treaties between EU member states and non-EU states. Since then, Richard (no doubt with the help of others) has identified the following treaties: Germany with Iran (1929), the CIS and other USSR succession states (1958) and Turkey (1929); Austria with Iran (1959), the CIS and other USSR succession states (1958), Balkan states (1954), Tunisia (1977) and Turkey (1989); Italy with Turkey (1929), Switzerland (1868) and Peru (1874); Estonia, Latvia and Lithuania with CIS (1993) and Ukraine (1995) and others; France with Denmark (1742), the Dominican Republic (1882), Iran (1885), Cambodia (1949), Tunisia (1957), Algeria (1962) and Togo (1963); and Greece with the Czech Republic and Slovakia (1927), and Switzerland (1927)

However, other inconsistencies remain: for example, in both cases, habitual residence will be a potential connecting factor. Although the Succession Regulation does not define 'habitual residence', it is likely to refer to the autonomous meaning developed through EU case law. The same centralised EU definition will not apply to the Hague Convention and so it is conceivable that a different result would be achieved despite the identical wording.

APPLICATION OF THE SUCCESSION REGULATION IN THE UK, IRELAND AND DENMARK

Contrary to a common misconception, the Succession Regulation has the potential to affect the estates of any individuals (regardless of where they are resident, domiciled or nationals) with any connection to any of the 25 EU member states in which the Succession Regulation has direct application. This will include individuals resident in the UK, Ireland, Denmark or even someone living outside the EU altogether.

Let us take the example of Sarah, a British citizen who is habitually resident in England and would like to take advantage of the Succession Regulation by circumventing French forced heirship and instead leaving her French holiday home to her brother (and not to her spouse and children).

Historically, the law that governs succession to the French house will most likely have been the *lex situs*: that of France. For a death after 17 August 2015, this may no longer be the case; article 21(1) tells us that: 'Unless otherwise provided for in this Regulation, the law applicable to the succession as a whole shall be the law of the State in which the deceased had his habitual residence at the time of death.' Article 22 goes on: 'A person may choose as the law to govern his succession as a whole the law of the State whose nationality he possesses at the time of making the choice or at the time of death.'

WHAT WILL THIS MEAN IN PRACTICE?

Unfortunately, if Sarah simply relies on her habitual residence to apply English law, the analysis is not entirely straightforward. Although article 21(1) seeks to apply the law of habitual residence, this remains subject to the application of *renvoi* (i.e. a reference on to the law of another jurisdiction). *Renvoi* is disapplied between member states but article 34 confirms that *renvoi* will still apply when habitual residence is in a third state and its law provides for a reference to be made to the law of a member state. This leads us to one of the key unresolved questions: is England (and the rest of the UK, Ireland and Denmark) a third state or a member state for the purposes of the Succession Regulation? Only if the UK is a member state (despite not signing up to the Succession Regulation) will *renvoi* be disapplied in this scenario.

If she is well advised, Sarah will not rely on English law applying by virtue of her habitual residence in England. *Renvoi* is specifically disapplied when a choice of law based on nationality is made and so Sarah will achieve the greatest degree of certainty by choosing for the law of some part of Britain to apply. English law allows testamentary freedom, subject to the *Inheritance (Provision for Family and Dependants) Act 1975* (the 1975 Act), and so Sarah can leave her French holiday home as she wishes, including in the shares that would have applied under French law.

CHOOSING AN APPLICABLE LAW

To achieve certainty, then, it is important that individuals make sensible and informed choices about the law that will govern the succession to their estate. What should they be thinking about?

The only possible choice is that of the law of nationality and, as explained in recital 38, this is 'in order to ensure a connection between the deceased and the law chosen'. Where there is more than one nationality, any of them can be chosen.

Article 22(2) explains that the 'choice shall be made expressly in a declaration in the form of a disposition of property upon death or shall be demonstrated by the terms of such a disposition'. An express declaration is easy to envisage. In fact, the practice is in no way new: Switzerland and Italy, for example, already have equivalent provisions in their domestic law.

An implied demonstration might be as simple as a reference to the statutory provisions of that particular law. Many will already unknowingly have made a choice of law: article 83(4) allows that 'if a disposition of property upon death was made prior to 17 August 2015 in accordance with the law which the deceased could have chosen in accordance with this Regulation, that law shall be deemed to have been chosen as the law applicable to the succession'.

Using Sarah as an example, if she has an existing English-law will, with references to English statute, the widely drawn provisions of article 83(4) must mean that this will count as a choice for English law to apply to the succession of the French property.

DOES CHOOSING THE LAW OF NATIONALITY JEOPARDISE EXISTING PLANNING?

Simply being able to make the choice of law does not mean that it is always the best option. As with any aspect of estate planning, adopting a wholesale, standardised approach can be risky and may inadvertently override any historic good planning.

For example, a long-term UK resident may have been advised to take advantage of an existing estate tax treaty by ensuring assets pass under a will governed by a particular law (i.e. the old UK-Indian and UK-Pakistan estate tax treaties, whereby clients domiciled in India or Pakistan can override the 'deemed domicile' provisions for UK inheritance tax by leaving their non-UK assets under a will not governed by any part of the UK). Although they may not be mutually exclusive, practitioners will need to weigh up the benefits of retaining any existing planning against the option of making nationality elections.

Another such example is the risk of disturbing planning done in accordance with existing private international law rules. The transitional provisions (at article 83(2)) preserve existing choices made before 17 August 2015 and in accordance with 'the rules of private international law which were in force, at the time the choice was made, in the State in which the deceased had his habitual residence or in any of the States whose nationality he possessed'. This can be of value. A common example is that of Italy: in certain circumstances, an Italian national can currently choose for the law of their habitual residence to govern succession. After 17 August 2015, this option will no longer be available for new wills and so any new planning may irrevocably upset the existing planning. In fact, the next few weeks represent a short window of opportunity to benefit from any such existing rules in domestic law.

Care must also be taken when more than one testamentary document is being prepared. A later choice of law can invalidate an earlier choice and so any such elections should be coordinated and carefully considered.

> **"Simply being able to make the choice of law does not mean that it is always the best option. As with any aspect of estate planning, adopting a wholesale, standardised approach can be risky and may inadvertently override any historic good planning**

DOES AN ELECTION REFER TO ALL OF THE DOMESTIC LAW OF NATIONALITY?

By making any such election (and in doing so disapplying *renvoi*), the testator is referring to the domestic law of the state of nationality. Presumably, this must mean the domestic law in its entirety, as it applies to the question of succession.

Article 23(2) lists the various aspects of succession that are relevant for these purposes, including (at paragraph (h)) 'the reserved shares and other restrictions... as well as claims which persons close to the deceased may have against the estate or the heirs'. Different EU states deal with the issue of protecting dependants and family members in different ways: while some states favour reserved shares for specific heirs, others prefer giving the courts jurisdiction. In England,[4] this consideration is dealt with by the 1975 Act: disgruntled heirs can apply to the courts for financial provision from the estate of an English domiciliary.

It has been suggested that an election for English (or Welsh) law to apply will include the 1975 Act. This must be correct. However, what is less certain is whether the 1975 Act will then apply to all British nationals with a connection with England or Wales, regardless of their domicile. Although others may disagree, it is difficult to see how the clear reference to a person 'domiciled in England and Wales' in the opening line of the 1975 Act can be overridden. It seems more natural that the 1975 Act will be included but will only apply if the testator was also domiciled in England or Wales. However, does that then mean that a French domiciled, dual French/British national, for example, can elect for English law to apply (thereby avoiding both the 1975 Act

4. The 1975 Act applies in Wales to Welsh domiciliaries, as well as England. It does not extend to Scotland or Northern Ireland

and French forced heirship rules) and disinherit dependant family members?

THE ROLE OF EXECUTORS

The chosen applicable law will also govern the role of 'the executors of the wills and other administrators of the estate' (paragraph (f) of article 23(2)). Some EU states already recognise the role of executors, others do not; this in itself can lead to difficulty.

To use an example, consider an election for English law to apply to French real estate. As examined above, an election for English law to apply will extend to all English domestic law related to succession, including the appointment of executors (for which, see the *Administration of Estates Act 1925*). So, by making an election, the French land may vest automatically in an executor, who may or may not also be an heir.

In practice, this may raise various practical difficulties, including taxation, registration and identifying suitable executors. How will the executor's role be treated for tax purposes? Would an executor be taxed at a higher rate than a close heir? Would the executor's role be treated as that of a trustee, giving rise to the associated tax and reporting requirements? Can the executors be given comfort regarding the deceased's liabilities?

Given these uncertainties, it may prove difficult to find people willing to act as executors in some cross-EU estates.

THE COUNTDOWN BEGINS

In the context of making estate planning easier for most people, the Succession Regulation is a good thing. However, various areas of uncertainty remain. Unless further guidance is issued in the next few weeks, this uncertainty is likely to continue until the CJEU is in a position to provide judicial interpretation.

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In search of John Banks

A tale of madness, consumption and 'incest' among the family involved in the landmark testamentary capacity case of Banks *v* Goodfellow

By Martyn Frost, Stephen Lawson and Robin Jacoby

Abstract

- **The seminal case of *Banks* v *Goodfellow* has shaped the law of testamentary capacity in common-law jurisdictions for over 100 years.**
- **While the legal implications of the case are well known, the story behind the case has been forgotten.**
- **This article documents the life histories of the Banks and Goodfellow families, focusing on the sad tale of John Banks and Margaret Banks Goodfellow, and the strange fate of the defendant.**

The appeal judgment in *Banks* v *Goodfellow* has remained a cornerstone of the law of testamentary capacity in England and Wales for almost 150 years.[1] It has a similar authority in many other jurisdictions, where the law derives from the common law. Often with law reports, the cast

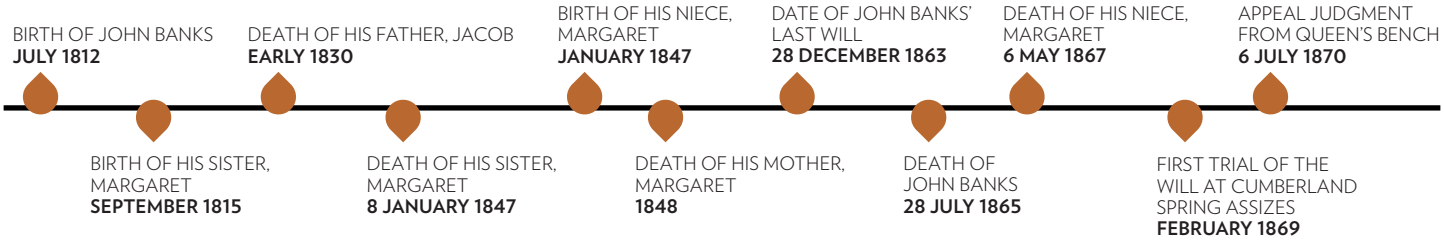
1 (1870) LR 5 QB 549. The court consisted of a panel of four judges:
Cockburn CJ (1802–1880): Sir Alexander Cockburn Bt was the Chief Justice of the Common Pleas, later Chief Justice of the Queen's Bench and in 1875 the first Lord Chief Justice. He had been an MP, Solicitor General and Attorney General before being appointed to the bench. He died in office. He was a womaniser who fathered two illegitimate children and had a temper so short that he seemed to some to be mentally unbalanced. Queen Victoria vetoed the traditional peerage given to a new Chief Justice, observing 'this peerage has been more than once previously refused upon the ground of the notoriously bad moral character of the Chief Justice'. As an advocate, he had already made his mark in the area of partial insanity in his successful defence of Daniel M'Naghten (see the final section of this article). His 1856 knowledge of poisoning from prosecuting the Rugeley Poisoner case would have been less useful and so would have been his long-lasting definition of obscenity in *R* v *Hicklin* (1868): 'Whether the tendency of the matter charged as obscenity is to deprave and corrupt…'

Sir Colin Blackburn (1813–1896): later Baron Blackburn, Lord of Appeal in Ordinary and Privy Councillor, notable for sitting in the House of Lords for the appeal in *Rylands* v *Fletcher* (1868).

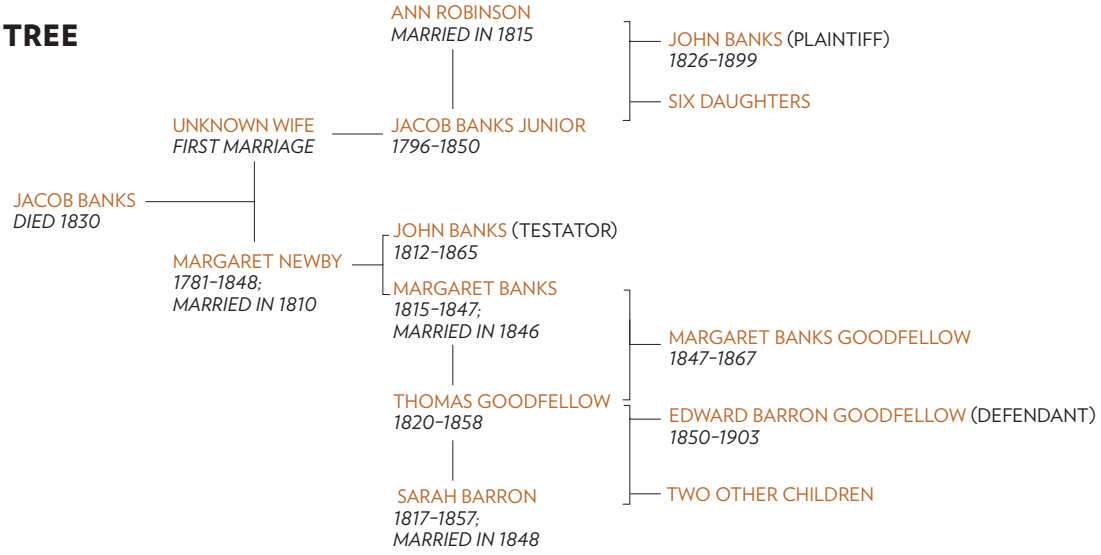
Sir John Mellor (1809–1887): judge of the Queen's Bench, and later Privy Councillor. He was, with Cockburn CJ, one of the panel of judges in the Queen's Bench that heard the second (criminal) Tichborne claimant trial (*R* v *Castro* (1874)).

Sir James Hannen (1821–1894): judge of the Queen's Bench, later of the Court of Probate and the Court for Divorce and Matrimonial Causes, then President of the amalgamated Probate, Divorce and Admiralty Division ('wills, wives and wrecks'), and later a Lord of Appeal in Ordinary and created Baron Hannen. He made a further significant contribution in the area of capacity with his summing-up for jury in *Parker* v *Felgate* (1883) that formulated what is known as 'the rule in *Parker* v *Felgate*'. He also presided over a significant undue-influence matter in *Wingrove* v *Wingrove* (1885)

TIMELINE OF KEY EVENTS



FAMILY TREE



of characters and their personal stories are lost when it comes to the statement of law. *Banks* v *Goodfellow* is no exception. The name of John Banks endures, but only because of his will and his illness. Twenty-eighth July 2015 is the 150th anniversary of his death and this has prompted us to try to rescue, to some degree, the circumstances of John Banks and his family from their present obscurity.

WHO WAS JOHN BANKS?

John Banks was the son of Jacob Banks, a black-lead pencil manufacturer in Keswick, Cumberland.[2] Jacob had married his second wife, Margaret Newby, in Kendal on 29 May 1810. There were two children from this marriage, John and Margaret. John was baptised at Crosthwaite Parish Church, Keswick, on 6 July 1812 and Margaret was similarly baptised on 19 September 1815.

Jacob Banks appears to have been one of three pencil manufacturers in Keswick in 1811.[3] He died in 1830, and, under the terms of his 1824 will, his wife received a life interest in his estate. After her death, the personal estate was to pass equally to his daughter, Margaret, and his son, John, after payment of GBP200 to Jacob Banks junior, who was the son from Jacob senior's first marriage (he was also a pencil manufacturer – see below, in the section regarding the plaintiff).[4] Jacob's real estate was divided, after the end of the life interest, between Margaret and John by specific gifts of designated properties.

2. The pencil industry had long been associated with Cumberland, where there were substantial graphite deposits. England enjoyed a monopoly on the manufacture of lead (graphite) pencils until well into the 19th century

3. *Jollie's Cumberland Guide and Directory* of 1811, quoted in 'The characters and events that shaped Keswick's pencil industry' by Dr Roger Asquith in the February 2011 issue of *The Journal of Lorton & Derwent Fells Local History Society*

4. If there was further issue of this first marriage, it is unlikely that they survived, as Jacob Banks senior only named Jacob junior, John and Margaret as issue in his will

No record has been found of John ever working, but this is not surprising given what we now know about his mental health. He appears to have been supported after the death of his mother, probably in 1848, by living off the rents of 15 cottages in Keswick.[5] The properties came to him from his father's estate, after the death of his mother, the life tenant. During the first trial of his will, these properties were reported as being worth between GBP1,000 and GBP2,000.

There is a reference to a John Banks in the 1841 census and it is most likely that this is the John Banks of this history.[6] He was then living with his mother, Margaret,[7] and sister, also Margaret, at Showley Crow in Keswick. Showley Crow is almost certainly the property that is today known as Shorley Croft on Penrith Road in Keswick (read more on this property in the section on Margaret Banks Goodfellow).[8]

In the 1851 census, John is noted as a visitor at Harryman Field, Keswick, the home of Joseph Usher, a pencil manufacturer.[9] John was then 38, unmarried and described as a 'proprietor of houses'. Evidence given at the trial at Cumberland Spring Assizes showed that John was a lodger at this property for some time. Joseph Usher's reported evidence was: 'My wife knew how to drive a bargain. What she said you might depend she would stick to. (Laughter) She agreed with John Banks for 10s a week for board, washing, and lodgings. John Banks was very greedy for money. He kept books and referred to them when I reminded him of forgetting to pay me for work done to his property.' This evidence, while given for the plaintiff challenging the will, illustrates that John was not only capable of negotiating his board and lodging, but also that he understood the value of money and how to keep a record of it. More evidence was given that, with patience, John could deal with business and, at least for a time, act rationally.

John later lodged with Superintendent[10] and Mrs Bird (see below for evidence from Mrs Bird). John Banks left them and lodged elsewhere during part of the 1850s. He then returned for a second period with them in 1859. This period covered the death of Featherstone Alexander (who was the subject of one of John's delusions) in 1860, but John was no longer with them by the 1861 census. At the 1861 census, he was lodging with a farmer called Isaac Thwaites at Slack Houses, North Row, Bassenthwaite.[11] After this, he moved to Gill Foot Cottage,[12] Arkleby.[13] He lodged here with James Routledge, a grocer, and his family, until his death. Members of the Routledge family registered both John's death, and, later, that of his niece, Margaret. The evidence at the first trial, and the comments in the appeal judgment about John lodging with the Routledge family, suggest that this was a way of obtaining at least rudimentary care for someone who was not able to look after himself. John appears to have used this method of care from 1848 to his death.

John died on 28 July 1865 and his death notice in the *Westmorland and Kendal Advertiser* for 12 August reads: 'On 28th ult, at Arkleby, at the house of James Routledge, wherein he had long been an inmate, Mr John Banks, youngest son of the late Jacob Banks, pencil manufacturer, aged 53'. The word 'inmate' in this announcement stands out. As used today, it would suggest someone who was confined in some way, rather than merely a lodger. The word does have a less common, and older, meaning of one who lives with others in the same house. It is likely that it was used in this sense.

5. We know from the appeal judgment that, when John made his last will, the cottages produced a combined rent of GBP80pa, more than enough to support him in the mid-19th century. In 1851 he was paying 10/- per week for board lodging and washing. In 1865, the weekly wage of an agricultural labourer was 11/3d: historyofwages.blogspot.co.uk/2011/02/agricultural-labourers-wages-1850-1914.html

6. A problem with this census entry is that John and Margaret are both shown as 25, having been born in 1816. This is incorrect, as John was 29 and Margaret 26 (both ages were probably rounded downwards to the nearest five years)

7. Described as aged 60, having been born in 1781

8. This property is described now, on one letting agency's website, as a large period property. A 1787 map shows this property as Shooley Crow

9. Joseph Usher and his wife, Mary, both gave evidence for the plaintiff at the trial

10. Understood to be a local policeman Isaac Bird; in the 1861 census he and his wife, Margaret, lived at Market Hill, Wigton, and had three children, aged six or under

11. The census entry is for Thomas Banks, aged 48, born 1813 in Keswick and he is again a 'proprietor of houses'. The Christian name given must be an error given the other details. Residence at Bassenthwaite also matches the reported evidence of Mrs Bird at the trial

12. 'Gilfort Cottage' in the 1861 census is believed to be an error. The property was built circa 1847. An 1860 conveyance shows the sale to William Thirlwall of 'a dwellinghouse, shop and premises, complete with the shelves, pigeon cotes, counters, beams, nails, cupboards and other fixtures in and about the said shop' (information from the current owner of the property). William Thirwall was the brother-in-law of James Routledge and was also an executor of John Banks' will

13. Arkleby is a small hamlet in Cumbria on the B5301 a little over one mile south of Aspatria. In the time of John Banks, it was in the county of Cumberland (which disappeared after the *Local Government Act 1972* took effect in 1974)

Illness

John Banks' life was overshadowed by his mental illness. There is no evidence of any physical handicap and there are reports of him out walking in the Lake District around his various homes. During the first trial of the will, evidence was given by Joseph Usher that John Banks had been 'simple' as a child.[14] As an adult, he suffered from delusions that he was being pursued by devils or evil spirits, and, on occasions, he believed them to be visibly present.[15] Along with these delusions went a violent antipathy towards a local man, Featherstone Alexander, and the mere mention of this name would induce violent and irrational excitement in John. The belief that Featherstone Alexander was pursuing him continued throughout John's life,[16] notwithstanding that Featherstone died in 1860. Evidence at the first trial also revealed that John had a second delusion about a man called Dudlow, who, he claimed, was a good man who gave him good advice. There was mention in the appeal judgment of medical evidence of John's 'general insanity' from a doctor who treated him between 1856 and 1862. There was further evidence from a local clergyman to similar effect.

John is also known to have suffered from epileptic fits from at least September 1863 onwards,[17] and, during these fits, the same doctor who gave the trial evidence considered John unable to transact business.[18] We know from the appeal judgment that John was confined for a time in the county lunatic asylum earlier in his life.[19]

The first trial regarding the will was held at Cumberland Spring Assizes before Brett J.[20] Evidence was given by Mrs Margaret Bird that John had lodged with her in 1853 and that: 'He was very unruly, one night he pulled the grate out, observing that he was going up the chimney to catch the devil. (Laughter) Had frequently to go to the door to stop him. He used to promise to be quiet, but as soon as they went away he began again. Never knew him sensible for more than a few minutes. While Banks was living with witness the second time, Fetherstone Alexander died. Banks said it was a good job Alexander was gone, as he would not be tortured again. He had a delusion about Goodfellow.[21] Banks two or three times thought that he had killed the devil. (Laughter) Once he said he had killed the devil with a cream jug. (Laughter) Saw him once struggling on the floor, and on witness asking what he was doing, he replied, "I am choking the devil". (More laughter) He further observed "I have done for the devil at last". He forgetting, went out naked. Once she (witness) caught him dancing on the flower bed, and he said – "I have got Alexander here, and I am pushing him down a little further". After witness and her husband removed to Wigton, Banks came to their house one very stormy night, and said that the devils drove him along the road from Bassenthwaite to Wigton. He was then very cold.'[22]

Cause of death

The causes of John's death, on 28 July 1865, are recorded on his death certificate as 'Epilepsy, Insanity and Coma'. Two of these recorded diagnoses, insanity and coma, are not strictly speaking feasible causes of death. Coma is a state of unconsciousness that is caused by a very large number of underlying physical diseases, one of which

14. Joseph Usher of Harryman Field, Keswick, in whose house John Banks lodged in 1851

15. The point was made during the first trial that Martin Luther threw his inkstand at the devil when he believed that he had come to see him. Considering the founder of the Reformation to have been mad, because he saw the devil, would not have been acceptable and, therefore, the reference was intended to diminish the implications of seeing devils and demons

16. At the first trial, Joseph Tolson, one of John Banks' executors, said in his evidence that John was frightened Alexander would 'fash' him. 'Fash' in the Wiktionary is described as meaning 'to worry, to bother or to annoy'

17. The standard treatment was to apply mustard blisters, the aim being to irritate the skin, as it was thought that the subsequent discharge from the blister would be beneficial to a patient's health

18. Despite this view, the attorney, Mr Ansell, who took the will instructions, and Mr Tolson, who collected rents for John Banks, considered that John was capable of dealing with his own business affairs

19. In 1841, when John was confined, there was no Cumberland county lunatic asylum, and he was instead confined at Dunston Lodge, Whickham, Durham. Dunston Lodge was opened circa 1830 and took patients from Cumberland (a formal contract for this was in place by 1846). The Cumberland and Westmoreland Asylum near Carlisle was opened circa 1862

20. William Brett (1815-1899), later 1st Viscount Esher. He was a justice of the Court of Common Pleas, later Lord Justice of Appeal and Master of the Rolls. He had also served as Solicitor General in 1868. His wife, Eugenie, was alleged, by some, to be the illegitimate daughter of Napoleon Bonaparte (one modern website confuses this point by listing William Brett as the illegitimate issue of Napoleon)

21. This must be the journalist's error in using 'Goodfellow' instead of 'Alexander'. John Banks is not known to have had any delusions about his Goodfellow relatives. This mistake is repeated in the report in the *Cumberland Pacquet*, 23 February 1869

22. The *Paisley Herald and Renfrewshire Advertiser*, 27 February 1869 (the same report had appeared in the *Glasgow Daily Herald*, 20 February 1869). These were presumably syndicated reports and look to be taken from a longer report in the *Cumberland Pacquet*, 23 February 1869

John Banks' mental disorder was characterised by delusions and probably also by hallucinations – he talked of being pursued by devils, one of whom was up the chimney

could have been the real cause of John's death. Insanity of itself cannot be a direct cause of death: it is related to causes of death through, for example, suicide or inanition. As regards the latter, before the days of antidepressants and electroconvulsive therapy, some patients would be so depressed that they starved themselves and went into a state of stupor (mental inaccessibility). They could literally starve themselves to death or develop a fatal pneumonia due to their weakened physical state.

How would this mental history be viewed today?

John Banks' mental disorder was characterised by delusions and probably also by hallucinations – he talked of being pursued by devils, one of whom was up the chimney. The modern diagnosis would most probably be paranoid schizophrenia.[23] However, bipolar disorder should not be ruled out. He was morose at times and said he was dead (consistent with depression). At other times, he was disinhibited and disturbed at night (consistent with manic behaviour).

If it is correct that the epilepsy came on years after the schizophrenia, when he was 52 or 53 and 21 months before his death, then it was probably unrelated to the mental disorder. A possible cause of the fits would then be a space-occupying lesion in the brain, such as a brain tumour or cerebrovascular lesion. It could have been due to a head injury, but we have no history of head trauma, other than self-inflicted, which caused bruising, but probably nothing more serious. Another likely disease to consider is tertiary syphilis, which was very common in those days, before the discovery of penicillin. Tertiary syphilis could cause psychosis, epileptic fits and dementia. There are other less likely causes. One possibility is a hydatid cyst in the brain. Hydatid disease is caused by a type of tapeworm, *Echinococcus granulosus*, and is rare now in the UK because modern hygiene is better than in the mid-19th century. It is commonly caught from sheep via dogs. One has to recall that Cumberland has always been sheep country, so this would not be a totally unreasonable diagnosis.

It is possible that the epilepsy came on before the mental disorder, although the evidence is against it, but, if the fits were what are known as 'absence seizures', others could have been unaware of them. In that case, the mental disorder might be connected. Early onset epilepsy is more likely to be idiopathic, meaning that there is no known cause. It is now recognised that longstanding idiopathic epilepsy can be associated with all sorts of mental disorders, of which schizophrenia is definitely one. Although idiopathic epilepsy usually comes on before the age of 50, it can begin at a later age.

Buried

John Banks was buried in Crosthwaite Parish Church, Keswick,[24] on 31 July 1865.[25]

THE WILL

John Banks had executed a will in 1838, leaving his estate to his sister, Margaret, who died in 1847. He decided on a new will in 1863, and two wills were prepared and executed in December of that year. His solicitor, Mr Ansell, and Joseph Tolson, John Banks' rent collector, travelled from Keswick to Arkleby for this purpose. This was an arduous journey on bad roads through rugged countryside in winter weather, on 2 December.[26] It would have been undertaken on horse or by horse-drawn carriage. Because of the difficulties of travel, a will was written out and executed at John Banks' lodgings during their meeting. The intention was that a formally engrossed will would be prepared and brought over later, but, until then, the will of 2 December would cover the position in the event that anything happened to John. The engrossment was brought over to Arkleby by Joseph Tolson on 28 December 1863 and was duly executed.

There are significant differences in the evidence about the 1863 will. The witness statements from

23. The word 'schizophrenia' was not coined until 1908

24. Dedicated to St Kentigern (known as St Mungo in Scotland), the churchyard is notable for the grave of Robert Southey (1774-1843), a long-time Keswick resident, who was one of the Lake Poets and Poet Laureate from 1813 to 1843

25. Crosthwaite Parish Register 1865 (entry 996), where he is shown, incorrectly, as a resident of Keswick

26. 'The distance between Keswick and Arkleby is about 20 miles and the road was said to be bad', *Banks* v *Goodfellow* (1870) LR 5 QB 549 at 553

“Margaret Banks Goodfellow is an even more shadowy figure than her uncle. She outlived him by only a short period, dying of consumption on 6 May 1867 in Arkleby, aged 20

Mr Ansell and Joseph Tolson were relied upon by the appeal court. Mrs Routledge's evidence, as reported in the press at the time of the first trial, has significant differences, although what is reported in the press appears to be about the 2 December meeting and not the engrossed will.

Mrs Routledge's evidence was that the will was drafted and executed without instructions from John Banks. In a sense this does not matter, as the engrossed will was executed later and the evidence in the appeal judgment is that John Banks read the engrossed will through two or three times, and said it was alright, before signing it. Such concentration on John's part was not necessarily beyond him, as the will was less than a single page.

It is reported as being said by Mrs Routledge (who was asked to witness the 2 December will) that she did not think it right to do so because of John's unfitness. She reports Mr Ansell as advising her that it made no difference, as Margaret was the heir without the will. William Thirlwell, who, together with Tolson, witnessed the later engrossed will (and was an executor), was Mrs Routledge's brother and landlord. He did not, apparently, give evidence.

The *Cumberland Pacquet* in July 1870 carries a report of the appeal court judgment. It also refers to Margaret Banks Goodfellow being the heir at law, with the additional observation that 'it seems to have escaped all parties that the niece would have taken without the will'. This appears to reflect what Mrs Routledge claims that she was told.

This remark was based, presumably, on the point that, if the two wills made in December 1863 were invalid, Margaret Banks Goodfellow would still have been the heir at law on John Banks' intestacy (being a niece of the whole blood as opposed to the plaintiff being a nephew of the half-blood). If Margaret's inheritance on intestacy failed through her not attaining her majority, then John Banks (the half-nephew and plaintiff) was the heir at law of his half-uncle John.[27]

Alternatively, if the 1838 will in favour of John's sister, Margaret, was not destroyed, with *animus revocandi*, and was drafted in the usual manner in favour of Margaret, her heirs or assigns, John's estate would pass under its terms to her heir at law. The judgment does not offer any clue as to what happened to this will. Margaret's interest would have passed to Thomas Goodfellow as her heir, and in turn his heirs would be his three surviving children (which included Margaret Banks Goodfellow). It seems that the plaintiff's case could only have succeeded in producing an inheritance for him if the two 1863 wills were invalid, and the 1838 will was either shown to be invalid as well or had been revoked by destruction, while the testator had sufficient capacity. It is unlikely, if the will existed as at the time of the 1863 meeting, that John Banks could have revoked it with sufficient mental capacity if he lacked testamentary capacity.[28] However, at this remove, it is quite possible that we are missing something in mid-19th century succession law.

MARGARET BANKS GOODFELLOW: THE NIECE AND BENEFICIARY

Margaret Banks Goodfellow was the sole beneficiary under John Banks' 1863 will. She was the only child of his late sister, Margaret. Margaret Banks Goodfellow is an even more shadowy figure than her uncle. She outlived him by only a short period, dying of consumption[29] on 6 May 1867 in Arkleby, aged 20. She died at Gill Foot Cottage, where latterly she had shared her uncle's lodgings. In her short life, she must have had little real family life. She would not have known her mother or her grandparents, and her father and stepmother were both dead when she was barely 11. Margaret was buried in St Cuthbert's churchyard, Plumbland,[30] on 9 May 1867. This church is under half a mile on foot from Gill Foot Cottage, where

27. 'This possible consequence of Margaret Goodfellow dying without issue and intestate, does not however, appear to have presented its self to the mind of any of the parties at the time of making the will', *Banks* v *Goodfellow* (1870) LR 5 QB 549 at 554 – nor did the possibility of a young lady, possibly known to have consumption, dying while a minor appear to have occurred to anyone

28. The modern approach is that the two actions require the same level of mental capacity: *Re Sabatini* (1970) 114 SJ 35

29. Tuberculosis, recorded on the death certificate as 'phthisis'

30. Plumbland Parish Register, entry 670

she died. No other members of her family are buried there and there is no identifiable marker for her grave.[31]

Her mother, Margaret Goodfellow (née Banks), was born in 1815. She married Thomas Goodfellow on 16 March 1846 (he was a grocer and tea merchant in Keswick)[32] and she subsequently died giving birth to Margaret,[33] on 8 January 1847. Despite her stated age of 29 on her marriage certificate, Margaret was in fact 30 years and six months old when she married and over 31 when she died. She was five years older than her husband. She was perhaps eager to appear closer to him in age when they married (and at least appear to be under 30) by taking two years off her actual age. It is probably unfair to speculate, but it seems unusual that a woman who stood to inherit property had to wait until 30 to marry. Was the knowledge of her brother's condition something that deterred suitors, who thought such a condition might be capable of being passed to their children?

After Margaret's death, Thomas Goodfellow married Sarah Barron in early 1848. Sarah died in 1857 and Thomas died on 6 April 1858. From her father's second marriage, Margaret Banks Goodfellow had two half-brothers, Edward Barron Goodfellow (born 1850) and John Tolson Goodfellow (born 1853),[34] and a half-sister, Mary Michinson Goodfellow (born 1851). John Tolson Goodfellow has no real part in this story, as he died on 21 March 1865. There is much more to say about Edward later.

The 1861 census (the first after her father's death) showed Margaret Banks Goodfellow as a scholar boarding with a family called Watson,[35] in Eskin Place, Castlerigg, Keswick. Her half-siblings were shown in the same census year as living with their maiden aunt, Frances Barron, in Main Street, Crosthwaite, Keswick. Why were the children split up? Did Frances Barron, who was no blood relative to Margaret Banks Goodfellow, not want the responsibility of an 11-year-old girl in addition to the two nephews and a niece who were related to her by blood?

Did John take on responsibility for maintaining and educating his niece or was it done by her father's trustees? There might be a clue in Thomas Goodfellow's will. He bequeathed his real property to Margaret Banks Goodfellow, the extent and value of which is not known. It is likely from the terms of her father's will that the income from the property would have been sufficient to pay for Margaret Banks Goodfellow's lodging and education (see more below on the origin of this property). Her father concluded his will by requesting that John Banks 'look after' Margaret 'as well as his strength will allow'. In this context, 'look after' could possibly be significant. Was the consumption that would eventually kill her at 20 already apparent, and could 'look after', imply more than paying for lodgings and education for the child? If her consumption was already apparent, was the known infectivity a reason to split the children up? Did she eventually come to live with her uncle John after finishing her education, as she was known to require nursing as well? According to evidence at the first trial, both John and Margaret were able to travel the 24 miles to visit Carlisle on one occasion in the 1860s, so perhaps her disease may not have had too early an onset.[36]

The property left to Margaret by her father included Shorley Croft, which is specifically mentioned in the will. This is the house occupied by her mother, uncle and grandmother at the 1841 census. We do not know who owned the property in 1841, although it is quite conceivable that this was part of the real estate in Jacob Banks' estate that was held for the life interest of his wife. If this formed part of Margaret's share of the real estate on her mother's death, then, on her death in turn, it would be logical that it passed to her husband, Thomas, as her heir. The gift of his real estate to Margaret Banks Goodfellow showed him to be returning her mother's property to her.

None of the questions about Margaret's short life can be answered, as our knowledge of her is so

31. There is, however, a prominent marker just inside the churchyard gate to Superintendent Isaac Bird and his wife, Margaret. John was their lodger for a time and they both gave evidence for the plaintiff against the will

32. 1851 census

33. *Kendal Mercury*, 16 January 1847, records death 'in child-bed'

34. This middle name is interesting, as the rent collector for John Banks, and executor of his will, was Joseph Tolson. He was described in the probate as a grocer. Was he a friend or relation?

35. George Watson was 65 and a road surveyor. Margaret was the only boarder at that address

36. Probably by train from Aspatria station (1.3 miles from Arkleby), as it would have been too far to walk

little. There is something very sad about a young orphaned girl being split from her half-siblings and sent to a remote rural hamlet to live with her invalid uncle, only to follow him to the grave less than two years later. Given the nature of her illness and the lack of close family, her years in Arkleby are difficult to see as being a happy time – we hope her early childhood was better.

EDWARD GOODFELLOW: THE DEFENDANT

Margaret Banks Goodfellow was the sole beneficiary of John's will. On her intestacy, her closest relatives were her brothers and sister of the half-blood. John Tolson Goodfellow predeceased her without issue, so her estate would have passed to Edward Barron Goodfellow (but not Margaret Michinson Goodfellow, as the male line was then preferred to the female). Edward did not attain 21 until after the litigation was concluded.

As well as Margaret Banks Goodfellow's inheritance from her uncle, John, her estate would have been augmented by her inheritance from her father. Edward would then have inherited all of this, as well as his own half-share of his father's personal estate. While this was not a vast fortune, it should have been of significant benefit to him.

Nothing is known about the life of Edward Barron Goodfellow until he married Hannah Armstrong on 6 April 1875 in Crosthwaite; he was 25 and she was 21. Hannah died, childless, four years later. Edward later appeared in the 1881 census as a hotel keeper at the Borrowdale Hotel in Borrowdale, outside Keswick.[37] There is some evidence that this hotel was owned, or at least leased, at one time by Hannah's father and mother (who died in 1873 and 1881 respectively). It is reasonable to surmise that Edward was involved with the running of the Borrowdale Hotel when he married Hannah in 1875.

Also in the 1881 census, a Mary Armstrong was recorded as a barmaid at the Borrowdale Hotel. She was the younger sister of Edward's deceased wife, Hannah, and she was then aged 17. On 26 July 1882, Mary married Edward Barron Goodfellow in Carlisle.[38] On 8 August 1882, Mary gave birth to a daughter, Clara Frances Barron Goodfellow.[39] Clara was not baptised until 16 December 1888, in Workington, after her mother moved there. Were the local clergy in Borrowdale reluctant to baptise a child where they might not have known of the marriage and, therefore, suspected Clara to be illegitimate? In fact, Clara was illegitimate, as she was born of a relationship which made her parents' marriage void. The Church of England would have argued at the time that the relationship was incestuous by Church rules as well.

The marriage of Edward and Mary raises difficult issues.[40] Marriage to one's deceased wife's sister was a void marriage for most of the 19th century. Further, it was a marriage which the Church of England would not knowingly perform. The *Marriage Act 1835* provided that all marriages after that Act that were 'within the prohibited degrees of consanguinity or affinity shall be absolutely null and void to all intents and purposes whatsoever'.[41] A marriage to one's deceased wife's sister was at that time within this definition. For Edward and Mary to have gone through the ceremony of marriage, the prior marriage to Hannah and Hannah's relationship to Mary would need to have

> **"Clara was illegitimate, as she was born of a relationship which made her parents' marriage void. The Church of England would have argued at the time that the relationship was incestuous by Church rules as well**

37. Built in 1866, the hotel still exists: www.lakedistricthotels.net/borrowdalehotel/index.php

38. They were married by licence in Christ Church in Carlisle. Edward is not described as a hotel keeper of Borrowdale, but as a gentleman of Botchergate in Keswick (and also a widower). See the following footnote for the description he used when his daughter's birth was registered. Mary is shown as a spinster, of no occupation, of Keswick. The witnesses are William Hall McVitie and Mary McVitie of no apparent connection to the bride and groom

39. The birth certificate recites the mother as 'Mary Goodfellow formerly Armstrong' and Edward Barron Goodfellow is shown as 'Hotel Keeper'. Although the birth was on 8 August 1882, it was not registered until 19 September 1882. The place of birth and residence of the mother both show 'Main Street, Keswick'

40. Consequences of a marriage in contravention of the *Marriage Act 1835* would be the illegitimacy of the issue (in the 19th century there were no succession rights for illegitimate children) and the social stigma that would have attached to bastardy and concubinage (to use expressions from the 19th century)

41. The reference to prohibited degrees is important in this context as one of the passages relied on from the Bible was Ephesians 5–31 – 'and they two shall be one flesh' – interpreted as having the consequence that, if a man and wife were of one flesh, so they were with the spouse's siblings. Other passages in support of the Church's position were Leviticus 18–8 – 'None of you shall approach any that is near of kin' – and 18–16 – 'Thou shalt not uncover the nakedness of thy brother's wife'

been concealed from the minister who celebrated the marriage (was this the reason for marrying in Carlisle and not Keswick?). But what of those in Borrowdale who surely remembered the first Mrs Goodfellow, or were they not told of the marriage?

The *Deceased Wife's Sister's Marriage Act of 1907* was the result of over 60 years of campaigning for law reform in this area,[42] and thereafter it permitted a valid marriage to one's deceased wife's sister.[43] But, until 1907, such a marriage was void and would have involved false declarations in order to obtain the licence for the marriage. Currently, s3 *Perjury Act 1911* provides for up to seven years' imprisonment on conviction for making a false declaration knowingly and wilfully to procure a marriage and it is difficult to see the law in 1882 prescribing a lower penalty. Thomas must have made such a false declaration when applying for the licence under which he married Mary.

Edward and Mary had two further children, John Goodfellow (born 1883) and a child, possibly called Frederick, who died soon after birth in 1888. Mary Goodfellow is shown in the 1891 census as then married and living in Workington, Cumberland. No husband was present on the census. In the 1901 and 1911 censuses, she was still shown in Workington, but then described as a widow. Her surname had by now reverted to Armstrong and her two daughters both appear on the census as Armstrong and not Goodfellow.

Edward disappeared from English records after the 1881 census. He emigrated to New Zealand in 1887 and then appeared as a groom in Wellington in the 1890, 1896 and 1900 New Zealand electoral rolls. He is thought to have died in New Zealand in 1903, aged 53. If the information about emigration is correct, it looks likely that Edward left his family before the birth of his last child.

Why Edward left his wife and children and went to New Zealand cannot be answered. However, it seems a reasonable assumption that it was connected in some way with the discovery of the void marriage, or at least the threat of its disclosure, which would inevitably bring about disclosure of the false declarations at the time of marriage, when he would have concealed the identity of his first wife and that his new wife was her sister. The consequences, apart from the public notoriety of what had occurred, would have included a likely conviction and imprisonment for perjury. This conjecture is possibly strengthened by the abandonment of his name by his family later.

Alternatively, one might ask why, having inherited half of his father's estate, possibly something from his maiden aunt, all of John's estate and Margaret's own estate, he ended up working as a groom? Had the money gone in the classic Victorian connection of the sporting life, alcohol and gambling? For a hotel keeper, that would not be an uncommon fate. At this remove we cannot tell, but the inheritances do not seem to have brought him good fortune or lasting wealth.

JOHN BANKS: THE PLAINTIFF

John Banks (son of Jacob Banks senior) had an older half-brother, Jacob Banks junior, believed to have been born in 1796. Jacob Banks junior was, like his father, a pencil manufacturer.[44] In 1815, he married Ann Robinson and they had several children, all daughters (some of them died in infancy), apart from one son, John (born 1826), who was the plaintiff in this case. Jacob appears to have been declared bankrupt in 1835 or 1836.[45] Jacob is thought to have died circa 1850.

John Banks, the plaintiff, does not appear to have married. In 1861, he was a painter,[46] living with his

42. Gilbert and Sullivan were inclined to gently mock the long-running campaign against reform, when the Queen of the Fairies in *Iolanthe* sang: 'He shall mock that annual blister, marriage with deceased's wife sister.' But other observations showed much more vitriol in attacking the reform. In 1876, the *Saturday Review* opined that such marriages, if permitted, would be examples of the 'diseased craving for abnormal enlargements of personal liberty which is the seamy side of Liberalism'. *The Quarterly Review* in 1849 thought that 'even popular discussion of the subject… is an almost incalculable mischief. Thoughts which never would have occurred to the pure have been forced on the purest'. On yet another defeat for reform, *The Church Review* was moved to be '… thankful to say that incest is no danger of being legalised at present'. Matthew Arnold thought reform would lead to bigamy, polygamy and, *per* WE Gladstone, 'the more horrible forms of incest'. Parliament was assured the reform would lead to 'enormities among peculiar sects of Christians' (from ES Turner, *Roads to Ruin: The Shocking History of Social Reform* (Michael Joseph, 1950)). One is left wondering at the Victorian view of the world. The wealthier could evade this prohibition on marriage by marrying their deceased wife's sister abroad

43. The *Deceased Brother's Widow's Marriage Act* did not follow until 1921

44. Samuel Ladyman's *Thoughts and Recollections of Keswick and Its Inhabitants During Sixty Years* (privately published, Keswick, 1885) lists Jacob Banks senior and junior both as pencil manufacturers 'sixty years ago', i.e. circa 1825

45. *Pigot's Directory of Cumberland* 1834 shows Jacob as a pencil manufacturer

46. The census entry reads 'Retired Painter'. At 34, he seems to be too young to have retired in the sense that it would usually mean today. Given that the next census describes him as a painter, it is tempting to think that the 'retired' refers to having left a regular occupation in order to paint. The National Portrait Gallery has a portrait of Francis William Newman (1805–1897), younger brother of Cardinal John Henry Newman (1801-1890), signed 'J Banks Ambleside'. The portrait appears to have been

maternal uncle, William Robinson (another pencil maker). In 1881, he lived alone in Crosthwaite and was described as a landscape oil painter. In 1891, aged 64, he lodged in Church Street, Keswick, and is described in the census as 'living on his own means'.[47] His three sisters who survived infancy, Emma, Anna Bella and Lavinia, all appear to have emigrated to the US. It is quite possible that John spent some time with them there. Evidence at the first trial was that his uncle, John Banks, had talked of going to see his nephew in America in order to avoid the evil spirits that tormented him (he said they would not follow him as they could not swim).[48] This is estimated to have been in the early 1860s.

John Banks died on 19 May 1899, aged 73. He directed in his will that he should also be buried in Crosthwaite Parish Church. His will directed that his estate be held on trust for income to be accumulated for 21 years,[49] and after that date the trust fund was to be distributed equally between his nephews and nieces. The will refers specifically to the ownership of rented properties, as well as dividends from three banks and shares in the Central Pacific Railway of California. He had prospered to a reasonable degree as an artist, unless this wealth came in part from inheritance from his mother's family.

"There seems to be nothing in Featherstone Alexander's personal details that would account for John Banks' aversion to him. Given that they were near contemporaries, is it possible that the animosity went back to childhood and school?

For a family that had, in all likelihood, suffered through their father's bankruptcy, the prospect of the 15 cottages in Keswick must have been quite enticing, but ultimately costly after two lost trials.

FEATHERSTONE ALEXANDER: THE 'PERSECUTOR'

The Featherstone Alexander who so haunted John Banks did exist, and we believe him to be Featherstonhaugh Alexander,[50] a grocer and tea dealer, who appeared in the 1851 census at 62 Main Street, Keswick. Thomas Goodfellow, John's brother-in-law, was also a tea dealer and grocer resident in Main Street, but whether or not there is anything significant in respect of John Banks' delusion in this coincidence is impossible to tell. Mr Alexander is also listed in an 1855 guide, which covers Keswick, as a grocer.[51] Featherstone Alexander married Susanna Hopper on 28 March 1842 and died in Keswick on 24 June 1860. There seems to be nothing in the personal details, that we know of, that would account for John's aversion to him. Given that they were near contemporaries, is it possible that the animosity went back to childhood and school?

VALEDICTION

This then is as much as we have been able to draw together from reports and records of the Banks and Goodfellow families' history around the time of the trial. The central characters were a mentally ill middle-aged man and a consumptive young woman. Neither appears to have had much joy in their lives, with no close family around them, relying instead on paid comfort (such as it was) from strangers. Incurable disease and deaths at early ages (at least by our standards) were very much the lot of many Victorians. Historical events do not necessarily pick those who look or act like heroes but here John and Margaret's joint legacy from their disease and death is a legal test that still

drawn from a photograph. It is quite possible, but far from certain, that this is the work of John Banks

47. His fellow lodger at that time was Richard Pendlebury, aged 44, described as 'Fellow & Lecturer of a Cambridge College'. He was a mathematician, collector of books (later donated to St John's College) and of musical manuscripts (which led to the foundation of the Cambridge Music Faculty Library). In addition, he was a famous Alpine climber (the first ascent of the eastern wall of Monte Rosa (1872)). He was born in Liverpool in 1847 and died in Keswick on 13 March 1902. Presumably he was lodging in Keswick, at the time of the 1891 census, for the hill walking

48. Evidence for the plaintiff of Mary Thwaite, John Banks' landlady in Bassenthwaite, quoted in the *Cumberland Pacquet*, 23 February 1869

49. And charged during this period with 20/- per week annuities to his three sisters

50. The name is given as Featherstone Alexander in the judgment, as Fetherstone Alexander in a press report and Featherstonehaugh Alexander in a census. If the latter is correct, it raises the question of pronunciation – was it pronounced Fanshaw? That the shorter Featherstone (as in Featherstone Rovers RLFC) was used tends to point against Fanshaw/Fanshawe. Curiously, a newspaper report of the appeal judgment gives the name as Featherstonehaugh, although that is not how the judgment sets it out

51. Harriet Martineau, *A Complete Guide to the English Lakes* (London, Whittaker and Co, 1855)

bears their families' names. We are sure they would have swapped their fates for more normal and fulfilled lives and who could blame them? However, we remain grateful to them for the sensible piece of law that arose from their deaths.

POSTSCRIPT ON THE LAW

It appears from a contemporary press report that the parties to this action had already skirmished in the Court of Chancery before this action. Chancery had directed that the action on validity be commenced at the Cumberland Assizes. Additional costs were therefore incurred over and above the costs of these two trials. Probate had been granted to the will on 29 August 1865, without challenge. It was the death of Margaret Banks Goodfellow in May 1867, and John Banks' assets passing to the Goodfellow family, that prompted the challenge to the will. The action is one described as 'ejectment' in the headnote to the appeal judgment.[52]

Exchanges at the first trial between judge and learned counsel for the plaintiff reveal a sharp divergence of views on the question of insanity and lucid intervals. It was reported in the *Cumberland Pacquet* on 23 February 1869 as follows:

'The judge reminded learned counsel that the only question was whether the testator was in a sound state of mind when the will was made...

'Mr Aspinall: There is a difficulty, my lord, which does not strike one at first sight. It is not a question whether this man had rational moments, but what was the general state of his mind.

'The judge: Well, the evidence goes to show that from time to time he was insane, no doubt. That is admitted.

'Mr Aspinall: My case is that he was in a state of chronic imbecility.

'The judge: Your own witnesses say that occasionally he could conduct business. He might be so when the will was made. Your case is prove the contrary.

'Mr Aspinall: I venture to submit not, my Lord. Every man in lunatic asylum may at times be in a state of mind fit to transact business.

'The judge: They might make a will during lucid intervals.

'Mr Aspinall: Lucid intervals is a term which requires a great deal of definition. With all deference to your Lordship, we will go on.'

What this was about is where the law on testamentary capacity stood in 1869. It was said in the appeal court in *Banks* v *Goodfellow* that 'in our day the doctrine has sprung up of the unity and indivisibility of the mind, but the ground on which insanity should cause incapacity appears to have been overlooked in the reasoning on which it is founded'.[53] The Privy Council, in *Waring* v *Waring,*[54] had previously followed the then fashionable doctrine of the unity and indivisibility of the mind, which maintained that any unsoundness of the mind, no matter how slight or unconnected with the will, was sufficient to prevent testamentary capacity being present. We now find it to be quite a reasonable view, on the part of Brett J, that a will in a lucid interval can be valid, but learned counsel seemed to doubt that this view conformed to the then existing law.

The jury retired for only 25 minutes before finding for the will. It was by this time half past eight at night and one wonders if there was an element of hunger that speeded up the verdict. After the jury returned there followed this exchange:

'Mr Aspinall: May I ask your lordship to stay execution?

'The judge: In order that you may move for a fresh trial?

'Mr Aspinall: I think that will be the course.

'The judge: Very well.'

Brett J is not apparently surprised at the request. That then set the scene for a strong appeal court in the Queen's Bench (see footnote 1 for the composition of the court). The appeal judgment in favour of the will, a clear and unanimous view, was that the law had taken a wrong turn with *Waring* v *Waring* and that a more rational test must be set out. Had members of the appeal court been looking out for a case such as this? Were they ready and waiting for the chance to steer the law back onto a more reasonable course? If so, Mr Aspinall QC does not seem to have suspected what lay in wait for him.

As well as upholding Brett J's application of the law, the appeal court also refused a retrial, taking

52. The action at common law to recover possession of land, as well as damages and costs for the wrongful withholding of the land: *Jowitt's Dictionary of English Law*, 3rd edn (Sweet & Maxwell)

53. (1870) LR 5 QB 549 at 563

54. (1848) 6 Moo PC 341; see also *Smith* v *Tebbitt* (1867) LR 1 P&D 437

the view that, if faced with the same evidence, another jury would find exactly as the Cumberland Assize jury did, particularly 'as to the absence of all connection between the delusions and dispositions made by the testator'. As a consequence, it would be 'worse than useless to put the parties to the expenses of a new trial'.

It does not seem to us to be a coincidence that Cockburn CJ chose to preside in this appeal. He had previously, and famously, made a name for himself in the area of partial insanity with his successful defence of Daniel M'Naghten.[55] His argument for acquittal was based on M'Naghten's partial insanity making him not responsible for his actions when acting under the influence of his delusions. This ran counter to the existing approach to insanity in the criminal law. Both his arguments in defence of M'Naghten and his later judgment upholding John Banks' will display the same understanding, supported by extensive quotations from the literature at the time, of mental illness. By the strangest of coincidences, John Banks and Daniel M'Naghten both suffered from paranoid delusions and were almost exact contemporaries. M'Naghten was born in the year following John Banks and he died two months before him.[56]

In a retrospective of Cockburn's career, in the *Harvard Law Review* of June 1900, the author drew attention to Cockburn's work on the doctrine of partial insanity, linking his defence of M'Naghten with the *Banks* v *Goodfellow* judgment, which the author described as 'beyond doubt one of Cockburn's most important judicial efforts'. Perhaps Cockburn CJ is the real hero of this story. In achieving fundamental and long-lasting change to the judicial view of insanity, in both criminal and civil law, he contributed significantly to moving the law on insanity in a more modern direction. For one man to have brought about these changes through the court in two important areas of law is an achievement that should not be underestimated. His arguments on both occasions show a greater understanding of issues of mental illness than was generally the case in his time. His approach was also far more humane and respectful of the individual's rights.

"Perhaps Cockburn CJ is the real hero of this story. In achieving fundamental and long-lasting change to the judicial view of insanity, in both criminal and civil law, he contributed significantly to moving the law on insanity in a more modern direction

The authors gratefully acknowledge the work that Title Research has kindly undertaken for us into the genealogy of the Banks and Goodfellow families. This assistance, particularly that of Claire Langford, has been invaluable and, without it, this article would not have been possible.

55. In 1843, Daniel M'Naghten killed while suffering from paranoid delusions. His victim was Edward Drummond, Prime Minister Robert Peel's private secretary. M'Naghten had mistaken Drummond for Peel. Cockburn ran a formidable, medically based defence which the prosecution could not counter. The key was whether or not partial insanity could be a valid defence. Although M'Naghten was said to be generally sane, Cockburn succeeded in showing that the paranoid delusions, under which M'Naghten was acting, made him not responsible for his actions. This decision ultimately led to the formulation of the M'Naghten rules (1843) on criminal accountability of the insane

56. In the newly opened Broadmoor Asylum

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Time to choose

The impact of the EU Succession Regulation on Italian trust and estate planning

By Maria Grazia Antoci and Daniele Muritano

Abstract

- ***Regulation (EU) No.650/12*** **(the Succession Regulation) will change Italian conflict-of-law rules. The connecting factor that determines the law applicable to succession will become the habitual residence of the deceased instead of the nationality of the deceased.**
- **The Succession Regulation will also change the criteria by which the choice of law governing succession is made, as it avoids *renvoi* and thus allows clients to plan their succession by choosing the law of their nationality.**
- **The *Hague Convention of 1 July 1985 on the Law Applicable to Trusts and on Their Recognition* (Hague 30) came into force in Italy on 1 January 1992. Italy recognises trusts as instruments of succession planning.**
- **Italy has a worldwide tax system. The Italian inheritance tax (IHT) regime is extremely favourable where succession involves the spouse and children of the deceased as heirs or legatees. The threshold under which no IHT is due is high, amounting to EUR1 million for each beneficiary.**

On 17 August 2015, *Regulation (EU) No.650/2012* (the Succession Regulation) will be wholly applicable. As this date approaches, lawyers are still struggling to clarify myriad unresolved issues regarding the new European succession system.

Italian conflict-of-law rules will undergo a big change, as the connecting factor that determines the law applicable to succession will shift. As a result, the Succession Regulation will have an impact on non-nationals who have settled in Italy (in most cases after they retire), as they will have the opportunity to plan their succession by choosing the law of their nationality; a choice that was not available before.

THE RULES APPLICABLE IN ITALY UNTIL 16 AUGUST 2015

The connecting factor

Until 16 August 2015, under Italian private international law (PIL),[1] the succession of a person will be governed by their national law at the time of their death. If the deceased has multiple nationalities, the law of the country to which they were mostly connected will apply; however, if one of these nationalities is Italian, Italian citizenship will prevail.[2]

It is important to note that the law applicable to the succession will govern all inheritance matters, from the opening of the succession to the division of the deceased's estate. The administration of the estate will, therefore, be included.

The choice of law

Professio juris is admitted under set and strict conditions.[3] In particular, the testator can choose the law governing their entire succession, but only the law of the state where they reside, provided that such a choice is expressed in the form of a will and the person is resident in that state at the time of death. No other kind of choice is admitted (implied choice, for example, is not allowed). As a result, if the deceased, at the time of death, has changed their residence, the choice of law will be ineffective.

Furthermore, with regard to the succession of an Italian citizen, the choice of law cannot affect the rights granted by law to Italian heirs who are resident in Italy at the time of death (the so-called forced heirship rights, which are usually granted only to the spouse and children of the deceased, but which may be granted, in certain cases, to parents or descendants of the deceased). The testator cannot, in any way, violate these rights unless the heirs are resident abroad at the time of the testator's death.

Renvoi

Renvoi back to Italian law made by the law of nationality of the deceased is accepted under Italian PIL. If there is a *professio juris*, *renvoi* is excluded.[4]

Under the present Italian PIL rules, *renvoi* will not operate if the law of residence is chosen. As a result, a British national residing in Italy could not choose English and Welsh (or Scottish) law as governing their succession, only Italian law (the law of the place of residence). *Renvoi* made by English and Welsh PIL rules (the law of nationality) back to Italian law, cannot be avoided by electing for English and Welsh law to govern the succession in the form of a will.

ITALY AND THE SUCCESSION REGULATION

Connecting factor

Under the Succession Regulation, the habitual residence of the deceased at the time of death will be the connecting factor. It will be the default rule to determine the law applicable to the entire succession. In other words, the applicable law will govern all questions related to the succession, from the start of the succession to the transfer of ownership of the assets forming part of the estate to the beneficiaries, including the administration of the estate.

Under article 21.1 of the Succession Regulation, the law of the state in which the deceased was habitually resident at the time of death might also be the law of a 'third state' (so-called *erga omnes* or universal application). If the law determined under article 21.1 is the law of a state bound by the Succession Regulation, the existence of a uniform connecting factor will avoid any conflict of laws. On the other hand, when the law of habitual residence is the law of a third state, the PIL of that state should be considered. If those rules provide for *renvoi* either to the law of a member state or to the law of a third state that would apply its own law to the succession, such *renvoi* should be accepted.

Therefore, the meaning of 'member state' and 'third state' under the Succession Regulation must be established. For example, what about the EU member states that have not adopted the Succession Regulation? Are they 'member states' or 'third states'? As the Succession Regulation does not contain a definition of 'member state' (unlike other instruments of European private law and the Succession Regulation proposal), a future decision of the European Court of Justice will be required to solve this important matter of interpretation.

In this respect, recital 82 of the Succession Regulation indicates that the UK and Ireland are member states, despite these states 'not taking part in the adoption of this Regulation and... not [being] bound by it or subject to its application'.

1. Article 46 of *Law No.218/1995*
2. Article 19 of *Law No.218/1995*
3. Article 46 of *Law No.218/1995*
4. Article 13 of *Law No.218/1995*

The Succession Regulation should be workable and systematically coherent, so we tend to agree with those scholars who have underlined how the inclusion of Denmark, UK and Ireland among the 'member states' for the purposes of the Succession Regulation would lead to a lack of consistency. Until this problem of interpretation is resolved, we will surely face some practical problems. A possible way to reduce uncertainty is to advise clients to make a choice of law when possible and suitable. As we shall see later, *renvoi* is excluded if the deceased had made a choice of law in favour of the law of a third state.

Choice of law

The Succession Regulation allows the testator of the disposition of property upon death (DoPuD) to make a choice of law. Article 22 provides that the testator can elect the law of their nationality (or, if they have multiple nationalities, the law of one of their nationalities) at the time of choice or at the time of death (it will be important to clarify this point, because the choice will remain valid even if the testator loses or changes nationality).

The choice of law can be made expressly in a declaration in the form of a DoPuD or can be implied (i.e. demonstrated by the terms of such a disposition).

It is worth noting that article 83 of the Succession Regulation extends the range of valid choice of law that can be made during the transitional period: 'Where the deceased had chosen the law applicable to his succession prior to 17 August 2015, that choice shall be valid if it meets the conditions laid down in Chapter III or if it is valid in application of the rules of private international law which were in force, at the time the choice was made, in the State in which the deceased had his habitual residence or in any of the States whose nationality he possessed.'

Renvoi

As mentioned above, *renvoi* shall be applicable only if the law of habitual residence is the law of a third state. In the case of a choice of law made in a DoPuD, all states bound by the Succession Regulation shall apply only the substantial applicable law (i.e. PIL rules are excluded) and no *renvoi* shall be admissible.

> **"We tend to agree with those scholars who have underlined how the inclusion of Denmark, UK and Ireland among the 'member states' for the purposes of the Succession Regulation would lead to a lack of consistency**

The above rule applies in any case of choice of law (whatever the chosen law is – i.e. the law of a member state or the law of a third state). In fact, recital 57 expressly provides that: '*Renvoi* should, however, be excluded in situations where the deceased had made a choice of law in favour of the law of a third state'.

This begs the question: would the third state whose law has been chosen (e.g. the UK) respect such a choice, or would it apply any possible *renvoi* to another law provided by its PIL rules? An answer to this question should be given on a case-by-case basis, depending on the law chosen. In our opinion, conflict of laws cannot be avoided in principle.

A PRACTICAL EXAMPLE

Mark, a British national who had moved with his wife to Italy from England in 1998, died in Italy in 2014. Under article 46 of *Law No.218/1995*, English law applies to his succession. Mark's estate comprised a house and a bank account in Italy and a bank account in England. The *renvoi* to English law would include the conflict-of-law rules. The English PIL provides for two different connecting factors related to the nature of assets (real estate or movables). The succession of movables is governed by the law of domicile, while the succession of real estate is governed by the *lex situs* (*lex rei sitae* is the Latin expression used by civil lawyers). Therefore, Mark's succession of the house in Italy will be governed by Italian law (which accepts the *renvoi* back). Should Mark be deemed domiciled in Italy at the time of death, the succession of the bank accounts (in Italy and the UK) shall also be governed by Italian law. The application of Italian law, of course, implies the application of rules regarding forced heirship provided by Italian law.

Under article 46 of *Law No.218/1995*, Mark could not choose English law as the law governing

his succession in order to avoid the *renvoi* back to Italian law. Under the Succession Regulation, however, this choice would have been possible under article 22, as Mark is a British national. Italy, as a member state to the Succession Regulation, will be bound to respect such choice and no *renvoi* back to Italian law will be accepted under article 34.2.

The PIL rules of the third state (the UK in the example above) should apply only if the law applicable to the succession is the 'default law', that is the law applicable under article 21.1 ('the law of the State in which the deceased had his habitual residence at the time of death'), and not when the law applicable to the succession is expressly (or impliedly) chosen by the testator.

According to UK scholars and practitioners, the above choice should also be respected by the UK. Whether or not the European certificate of succession issued in Italy (the place of habitual residence) will be accepted in the UK is an open issue. It is also questionable if the UK would respect the choice of national law made by an Italian national habitually resident in the UK. Would the UK apply Italian law to assets situated in the UK?

THE RECOGNITION OF TRUSTS IN ITALY

Italy has recognised trusts since the *Hague Convention of 1 July 1985 on the Law Applicable to Trusts and on Their Recognition* (Hague 30) came into force on 1 January 1992. The Convention was ratified by Italy in 1989.[5] Hague 30 contains a definition of 'trust' in article 2 'for the purposes of this Convention', which means that the definition is not identical to that of the English and Welsh trust. Italian scholar Maurizio Lupoi argues that the trust defined by article 2 of Hague 30 is a 'shapeless trust' because it refers not only to English and Welsh trusts but also to the so-called trust-like institutions, so Hague 30 may also apply to these kinds of legal institutions (e.g. foundations).[6]

"It is questionable if the UK would respect the choice of national law made by an Italian national habitually resident in the UK. Would the UK apply Italian law to assets situated in the UK?

Italy only recognises express trusts (*inter vivos* or *mortis causa* trusts) under article 3 of Hague 30, i.e. trusts created voluntarily and evidenced in writing. Constructive trusts, resulting trusts and implied trusts are outside the scope of the Convention. The Italian courts cannot 'create' a trust (e.g. where property is obtained or retained by unconscionable conduct).

Italy must address a number of problems around the recognition of trusts. First, for a trust to be recognised in Italy, it must be consistent with the provisions of article 2 of Hague 30: the assets must have been placed under the control of a trustee. For example, the US revocable trust (under s603 *Uniform Trust Code*, also called a 'living trust'), in which the trustee's duties run primarily, and perhaps even exclusively, to the settlor, does not appear consistent with article 2, because assets are not placed under the control of a trustee. A power of revocation, in fact, is the functional equivalent of ownership.

Another problem arises with regard to rights and powers retained by the settlor. Rights and powers reserved under the law governing the trust can in fact be inconsistent with article 2 of Hague 30 (e.g. the powers reserved by the settlor under s9A *Trusts (Jersey) Law 1984*). A trust in which the settlor reserves to themselves the powers provided by s9 *Trusts (Jersey) Law 1984* is probably not a trust 'for the purposes of the Convention'.

Under article 4, Hague 30 does not apply to preliminary issues relating to the validity of wills or of other acts by virtue of which assets are transferred to the trustee. These acts are governed by the *lex fori* – for example, if an English settlor wishes to transfer to the trustee an immovable asset located in Italy, a notarial deed must be used to register the transfer in the Italian Land Registry.

Since Hague 30 has come into force, Italian practitioners have begun to explore if the convention would allow the creation of trusts in the absence of foreign connecting factors, aside from the applicable law. A wide interpretation of Hague 30 led to the creation of the so-called 'internal trust' – i.e. 'a trust whose elements are all connected with Italy except for the applicable law, that is a law of a trust country'.[7]

5. *Law No.364 of 16 October 1989*

6. 'The Shapeless Trust', *Trusts & Trustees*, (1995), no.3, 15
7. Maurizio Lupoi, *Trusts*, (Milan, 2001), 536

In an internal trust, the settlor is Italian, the trustee is Italian, the assets are located in Italy, and the beneficiaries are Italian. The Italian court approved this experiment and now the creation of internal trusts is common in Italy. Statistically, the majority of internal trusts are governed by English and Welsh trust law or by the *Trusts (Jersey) Law 1984*, but sometimes professionals are unaware of the applicable law. The application of the wrong choice of law to the trust can result in critical situations.

Internal trusts may be classified as follows:

- **accumulation and maintenance trusts (i.e. discretionary trusts);**
- **trusts to preserve family-owned businesses; or**
- **trusts for persons affected by a disability.**

As for the assets of internal trusts, mainly the settlor entrusts real property (e.g. the matrimonial home) and shares in limited liability companies.

A number of succession issues arise from trusts operating in Italy. Article 15 of Hague 30, in fact, contains an important provision regarding the protection of heirs and legatees. Hague 30 does not prevent the application of provisions of the law designated by the conflicts rules of the forum, in so far as those provisions cannot be derogated from by voluntary act, relating to succession rights, testate and intestate, especially the indefeasible shares of spouses and relatives. This provision protects forced heirship rules against family trusts.

Trusts cannot withstand a challenge in court by a disappointed heir; this is a real limitation to the use of trusts in Italy. Therefore, if the succession is governed by Italian law, the trust may be successfully challenged in court. Yet, trusts in which some future heir of the settlor is not a beneficiary are very rare and the trust instrument contains clauses that dissuade the heir to challenge the trust, because they obtain more than the indefeasible portion. Case law considering trust and forced heirship is absent in Italy, except one case about jurisdiction, in which the Supreme Court stated: 'The agreement concerning jurisdiction (prorogation of jurisdiction clause) established in the trust instrument is not binding for a "third party" (i.e. someone who is neither the settlor, nor the trustee or the beneficiaries).'[8] This decision is very important and underlines that:

- **the prorogation of jurisdiction clause binds only the settlor, the trustee(s) and the beneficiary(ies);**
- **the prorogation of jurisdiction clause does not bind a 'third party' (e.g. a 'disappointed' heir); and**
- **it will be hard for the settlor to use a non-internal trust to undermine the rights of their forced heirs.**

INHERITANCE TAX IN ITALY

The Succession Regulation does not apply to revenue matters; national law determines how taxes and other liabilities are calculated and paid.[9]

Inheritance tax (IHT) and gift tax in Italy is governed by *Decree No.346 of 31 October 1990* and *Decree No.262 of 3 October 2006* (the Decree). Italy has a worldwide tax system. Therefore, if the deceased had their last residence in Italy at the time of death, assets will be liable for IHT irrespective of where they are located. If the deceased had their last residence abroad at the time of death, only assets located in Italy will be liable to IHT. Yet we need to consider the double-taxation agreement between Italy and the UK, which was signed in 1966 and came into force in Italy in 1967.[10] Moreover, under article 26 of the Decree, even if no double-taxation agreement exists between Italy and a foreign country, if the deceased had their last residence in Italy and owns assets abroad, taxes paid in that country may be deducted from IHT due in Italy.

The Italian IHT regime is extremely favourable where succession involves the spouse and children of the deceased as heirs or legatees. The threshold under which no IHT is due is high, amounting to EUR1 million for each beneficiary. Thus, if the deceased had a spouse and two children, the threshold amounts to EUR3 million. As a result, most successions are IHT-free. In addition, if a family-run business is among the assets (e.g. the majority of company shares), under certain conditions no IHT is due, irrespective of the value.

If the value of the assets exceeds the threshold, the IHT treatment is nevertheless low, as the IHT due amounts to just 4 per cent of the value exceeding the threshold. But, as mentioned

8. *Corte di Cassazione*, 20 June 2014, no.14041

9. Article 10 of the Succession Regulation

10. *Law No.793 of 9 August 1967*

previously, this situation is rare, so succession in Italy is mostly tax-free.

The Decree also provides for succession involving other relatives of the deceased or unrelated persons as heirs or legatees. If heirs or legatees are siblings of the deceased, the threshold is reduced to EUR100,000 for each beneficiary and the IHT due if assets exceed the threshold is 6 per cent on the whole value. If they are unrelated, no threshold is provided and the IHT is 8 per cent on the whole value.

Other types of taxes are due from heirs or legatees, but only with reference to immovables bequeathed to them. These taxes are due for the registration of immovables with the Land Registry and they amount to 3 per cent, calculated and paid on the fiscal (thus not market) value of the immovables (the so-called 'cadastral value'). As this value is usually one-third (or less) of the market value, these taxes are also low. Furthermore, if an immovable is classified as a 'first home', a fixed tax of only EUR400 is due.

TRUSTS AND INHERITANCE TAX IN ITALY

IHT in Italy is due on assets held in testamentary trusts and *inter vivos* trusts. The main features of IHT treatment of trusts are as follows:

- **irrelevance of the trustee for IHT purposes;**
- **relevance of the settlor-beneficiary relationship;**
- ***inter vivos* trusts are treated as a direct gift to beneficiaries; and**
- **the IHT thresholds are applicable to trusts, so the taxation is extremely favourable.**

Consider, as an example, a matrimonial home held on trust with a fiscal value of EUR500,000. If the beneficiaries are the settlor's spouse and children:

- **no IHT is due (because the fiscal value of the home is under the threshold);**
- **taxes due for the registration of property in the Land Registry amount to 3 per cent;**
- **the increase in the trust fund value is exempted from taxes.**

Surprisingly, in Italy, any disposition of law expressly provides for the application of IHT to trusts. The rationale for the application of IHT to trusts, according to Italian tax administration interpretative documents, is that an assignment of assets to beneficiaries through a trust is, for IHT purposes, an assignment of assets as through a will or gift.

CONCLUSION

This article examines some of the myriad issues emerging from the Succession Regulation. Many of the other issues will be addressed by professionals, scholars and judges. The Succession Regulation represents a real cultural challenge for those who deal with succession planning and winding-up of estates not only in EU member states, but also in third states. These debates are just the start.

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Commercial realities

To what extent can US commercial trusts mitigate investor risks?

By James J Holman

Abstract

- **Trust structures are used extensively in US commercial transactions, and are particularly common in large-scale asset-investment vehicles such as real estate investment trusts (REITs), asset securitisations, and municipal finance offerings.**
- **Notwithstanding the use of terms and concepts closely associated with the law relating to private trusts in some commercial structures, established practice also leads to hybrid vehicles that combine both traditional trust and corporate-law components.**
- **The closer that a commercial trust structure adheres to established state law cultivated in the private-trust context, the greater the likelihood that a court will apply traditional trust law in the commercial context.**
- **Courts faced with controversies arising under hybrid structures must often struggle to determine whether the parties to any given structure intended the fiduciary standards of state trust law to apply.**

Fiduciaries under trust structures are generally held to higher standards than the typical 'business judgment' standard applied under corporate law. As such, advisors counselling parties at the outset of a commercial transaction should carefully evaluate the governing jurisdiction and the structure of the asset vehicle itself to ensure that the structure has maximum stability and, where necessary, flexibility. Because of their flexibility, variety, and aura of fiduciary-guarded integrity, trust structures permeate many of the most sophisticated commercial investment vehicles now commonplace in the United States. Investors seeking diversification of assets, tax-advantageous returns, and protection from the variability of typical corporate governance often find such structures attractive. Notwithstanding these advantages however, the lack of flexibility in many trust vehicles has led to litigation, lower rates of return, and disparate treatment from state to state when legal enforcement becomes an issue.

As in the private client context, a high premium on predictability, ease in enforcement of trust documents, and protection of trustees and other trust fiduciaries often lead commercial parties to utilise specific, seasoned jurisdictions such as Delaware and New York. However, whatever the choice of law in any specific structure, the commercial trust, like its private client counterpart, can become immersed in litigation when administration, enforcement, or outside facts lead to outcomes that disappoint beneficiaries.

What follows is a discussion of the three most common contexts within which one is likely to find commercial trust structures at work in the US – asset securitisations, municipal bond facilities, and real estate investment trusts (REITs) – together with recent case law examples from each area that illustrate the vulnerabilities of fiduciaries and beneficiaries of these structures when commercial realities defy expectations arising at the outset of a deal.

THE REAL ESTATE INVESTMENT TRUST

The US Congress established the modern REIT with the passage of the *Real Estate Investment Trust Act of 1960*. The purpose of the Act was to create a passive investment vehicle for participation by average investors in a diversified real estate portfolio managed by professional managers. Through a REIT, individual investors are able to pool their capital to participate in large real estate ventures that would otherwise be cost-prohibitive. REITs are typically structured as trusts, with an independent trustee holding the REIT's real estate assets on behalf of unitholders as beneficiaries. Although a REIT may or may not actually use the strict trust form, the REIT trustee's duties are set forth in a trust deed or other trust agreement. The trustee is responsible generally for the safe custody of the assets. The trustee also monitors the REIT's compliance with applicable laws, oversees the actions of the REIT's management, and ensures fair treatment of unitholders as a whole.

In a typical REIT, money raised through a public offering of units similar to common stock is used by the REIT to purchase a pool of real estate properties (often from a sponsoring corporation, such as a developer). The real estate properties are then leased out to tenants, and the lease income flows back to the investors as income distributions or dividends. To ensure that the REIT remains a passive conduit, the properties are managed by an independent property manager, and the REIT itself is managed by independent management. Thus, REITs usually have annual manager's fees, property management fees, trustee's fees and other expenses that are paid out before distributions are made to investors. To encourage investment in REITs, the US Internal Revenue Service (IRS) provides these entities with favourable tax status, as long as they meet certain diversification benchmarks and other requirements, such as distributing at least 90 per cent of the REIT's income as dividends.[1] This non-entity tax status is the main attraction of REITs as an investment vehicle.

Most REITS actually use a corporate form, rather than the typical trust form. This can lead to questions about whether the REIT trustee's duties should be analysed under state trust law or corporate law. In *Stender* v *Archstone-Smith Operating Trust*,[2] the court considered whether a claim for breach of fiduciary duty by a REIT's trustee could proceed under state trust law or state corporate law.

1. US *Internal Revenue Code* (IRC) §§ 856(a), 857
2. 2014 WL 5152002 (District of Columbia, 2014)

Archstone REIT was the sole trustee of Archstone UPREIT (UPREIT), and responsible for UPREIT's strategic direction and property management. Archstone REIT also owned approximately 90 per cent of UPREIT's beneficial interests, in the form of A-2 common units. The plaintiffs held approximately 11 per cent of UPREIT, in the form of A-1 common units.

Archstone REIT entered a merger agreement with Tishman-Lehman Partnership (TLP), valued at approximately USD22.2 billion, which terminated the plaintiffs' A-1 units and required A-1 holders to choose between one of two options: a cash payout of USD60.75 per unit, or the equivalent number of newly created series O units. Following the merger, Archstone REIT, as majority shareholder, transferred billions in UPREIT assets to itself and then merged with TLP; the merged entity became the sole trustee of UPREIT.

The plaintiffs sued Archstone REIT both in its capacity as trustee of UPREIT and as the majority shareholder, arguing that Archstone REIT engaged in improper self-dealing and failed to take appropriate steps to ensure that the A-1 unitholders' rights were protected in the merger. The plaintiffs argued that the Series O units had inferior economic characteristics to the A-1 units, including possible loss of tax-deferred status. The plaintiffs also claimed that the 'sole purpose of leveraging the assets was to permit an impermissible distribution to the A-2 unitholders to fund the acquisition of the Archstone REIT'. Archstone REIT sought dismissal for lack of standing, citing the Maryland corporate code, which states: 'Nothing in this section creates a duty of any director of a corporation enforceable otherwise than by the corporation or in the right of the corporation'.[3] In response, the plaintiffs argued that Maryland corporate law is irrelevant because they brought the claim under Maryland trust law.

The court disagreed, finding that REIT trustees are functionally more similar to corporate directors than traditional trustees, and that Maryland courts have consistently applied Maryland's corporate law to issues involving REITs. Accordingly, the court held that a breach of fiduciary duty claim brought against the trustee of a REIT is governed by Maryland corporate law, rather than trust law, and that the plaintiffs, therefore, lacked standing to bring a direct action to enforce the defendants' fiduciary duties. However, the court held that the plaintiffs did have standing under corporate law to bring a claim for breach of Archstone REIT's fiduciary duty as majority shareholder.

"The court held that a breach of fiduciary duty claim brought against the trustee of a REIT is governed by Maryland corporate law, rather than trust law, and that the plaintiffs, therefore, lacked standing to bring a direct action to enforce the defendants' fiduciary duties

ASSET SECURITISATION

Asset securitisation involves the segregation of financial assets (like mortgages or accounts receivable) from the originating company's general business risks by transferring those assets to a special purpose entity (SPE), often taking the form of a trust. In turn, the administration and servicing of the assets is often subcontracted by the trustee back to an affiliate of the originator. The trustee is responsible for the ongoing administration of the SPE, as well as protecting the interests of investors who purchase the securities issued as a result of the securitisation.

The securitisation trustee's duties are set forth in a trust agreement. After closing, the trustee works with the servicer and other parties to administer the trust and ensure that payments are collected pursuant to the underlying financial assets and paid out to investors. If a party to the trust agreements breaches its obligations, the trustee takes on a more active role, notifying security holders of the breach and actively representing the interests of the security holders.

However, one of the trustee's most important duties is the initial duty of confirming that the trust has actually received good title to the assets being securitised, and that such title is clear of any liens or other claims, such as by creditors of the originating company. This is referred to as 'bankruptcy remoteness', which the trustee

3. Md Code Ann Corps & Ass'ns § 2–405.1(g)

Referring to *Glaski* as an 'outlier', the court noted that the majority of district courts in California have held that borrowers do not have standing to challenge the assignment of a loan because they are not party to the assignment agreement

ensures by requiring legal opinions that the security interest has been perfected and that title has been transferred.

Problems can arise when the trustee fails to properly monitor and ensure the transfer of the assets to the trust prior to closing. This has been an ongoing issue in the mortgage-backed securitisation context. In *Glaski* v *Bank of America, NA, et al*,[4] the California Court of Appeal for the Fifth Appellate District held that a borrower has standing to state a claim for wrongful foreclosure based on allegedly improper securitisation of the borrower's note and deed of trust. This case represents a minority view and has been criticised for a number of reasons. The Glaskis obtained a mortgage loan from Washington Mutual Bank, FA (WaMu), secured by a deed of trust against their residence and identifying WaMu as the lender and beneficiary. The Glaskis' note, along with many others, was purportedly securitised into the WaMu Mortgage Pass-Through Certificates Series 2005-AR17 Trust, created under New York law.

When the Glaskis defaulted under the note and deed of trust, Bank of America, NA, as successor trustee of the WaMu securitisation trust, began foreclosure proceedings and sold the Glaskis' property pursuant to the power of sale provisions in the deed of trust. The Glaskis responded by instituting a wrongful foreclosure proceeding against several defendants, including JPMorgan Chase Bank, NA, as acquirer of WaMu's interest in the subject loan, and Bank of America, as trustee. Among other things, the Glaskis asserted that the their loan was not transferred into the securitised trust before its closure date, in violation of the trust's pooling and servicing agreement, and that the defendants consequently had no right to foreclose under the deed of trust.

The court first held that the Glaskis had standing to challenge the foreclosure sale based on the untimely transfer of their note and deed of trust into the securitised trust. The court acknowledged that, in wrongful foreclosure cases based on ineffective loan assignment, the borrower often does not have standing to challenge the assignment of the loan because the borrower is not a party to the trust's pooling and servicing agreement. Nonetheless, the Court of Appeal reasoned that, where the asserted defect voids the assignment, as opposed to rendering it merely voidable, a borrower has standing to challenge an assignment of the borrower's note and deed of trust. Looking to New York trust law, the court determined that a transfer to a securitised trust after the trust's closing date rendered the transfer void. Consequently, the Court of Appeal held that the Glaskis had standing to challenge the foreclosure based on their allegations that the post-closing attempt to transfer their deed of trust and note into the WaMu trust was void.

Other courts have rejected the *Glaski* court's approach. For example, in *Sandri* v *Capital One, NA, et al (In re Sandri)*,[5] the facts were almost identical to those in *Glaski*. Just as in *Glaski*, the debtor-plaintiff challenged foreclosure proceedings against her residence, arguing that the securitisation of her loan failed because the attempted transfer took place after the closing of the securitisation trust, in violation of the trust's pooling and servicing agreement. However, unlike in *Glaski*, the bankruptcy court in *Sandri* dismissed the debtor-plaintiff's challenge to the foreclosure proceedings for lack of standing.

Referring to *Glaski* as an 'outlier', the court noted that the majority of district courts in California have held that borrowers do not have standing to challenge the assignment of a loan because they are not party to the assignment agreement. The court also flatly rejected the *Glaski* court's interpretation of New York trust law, stating that, in fact, New York courts have consistently found that transfers in violation

4. 218 Cal App 4th 1079 (Cal App 5th Dist 2013)

5. 501 BR 369 (Bankr ND Cal 2013)

of a trust agreement are voidable, not void. Accordingly, the bankruptcy court held that the debtor-plaintiff did not have standing to enforce the trust's pooling and servicing agreement because she was neither a party to the agreement nor a third-party beneficiary.

MUNICIPAL BONDS

Municipalities meet most of their capital needs by issuing bonds, secured either by the municipalities' general tax revenues or by the proceeds of the specific project being funded by the bond issuance. Most bonds are issued pursuant to a trust indenture, which is the agreement made between the issuer and the trustee that represents the bondholder's interests. The trust indenture highlights the rules and responsibilities of each party and explains the source of income for repayment of the bonds.

The typical indenture or trust agreement tasks the trustee with monitoring the debt service and collecting revenue for payment to bondholders. The trustee may also be responsible for ensuring that the bond proceeds are invested in accordance with the terms of the indenture or trust agreement. Common purposes for bond proceeds include servicing prior municipal debt or funding a specific infrastructure expenditure, such as a bridge. The trustee also represents the interests of the bondholders in the event that a party to the trust indenture breaches or otherwise fails to fulfil its obligations.

In *In re Delta Air Lines, Inc*,[6] the Kenton County Airport Board (KCAB) issued approximately USD400 million in municipal bonds to finance improvements at the airport, to be used primarily by Delta Air Lines. The bonds were issued under a trust indenture agreement between KCAB and UMB Bank as indenture trustee, and were guaranteed by Delta. Delta also executed a lease requiring it to make lease payments (assigned to the bond trustee) in an amount equal to the debt service.

In 2005, Delta filed for Chapter 11 bankruptcy protection, and made a motion to reject the lease. The parties ultimately reached a settlement in 2007, under which KCAB would renew the lease to Delta and issue new bonds to the bondholders in a reduced principal amount, and the indenture trustee would be allowed a USD260 million unsecured claim on behalf of the bondholders. The settlement, which required bankruptcy court approval, also sought several releases, including a release for the indenture trustee of all claims that might be brought by the bondholders against it.

The indenture trustee formed a bondholders committee, and sent out 16 separate notices to bondholders inviting them to join the committee, which ultimately consisted of bondholders holding 60 per cent of the bonds. The committee ultimately consented to the settlement by a vote of over 95 per cent. When Delta announced the settlement, but after the court confirmed the plan, a group of bondholders objected on the grounds that the bankruptcy court had no jurisdiction to impose a settlement releasing non-debtor third parties, and that the indenture trustee had no authority to bind dissenting bondholders to a settlement that reduced the principal and interest of the bonds.

The bankruptcy court found that, because (i) all bondholders had been given a chance to participate in the reorganisation proceedings, (ii) the settlement order was approved by final order of the court after the vast majority of bondholders had voted to accept it, and (iii) no effective relief could be granted to the dissenting bondholders without undermining the debtor's reorganisation, the dissenting bondholders' objections were 'equitably moot' – that is, not capable of being subject to a remedy the court could grant. On appeal, the district court affirmed the settlement order and agreed that the objections were moot, but addressed the bondholders' objections nonetheless. Addressing the jurisdictional objection first, the court held that the third-party releases were permissible because they were necessary to prevent subsequent litigation of the claims that were resolved by the settlement.

Addressing whether the indenture trustee had authority to impair the bondholder's rights to payment, the court first found that the indenture trustee had given the bondholders more than adequate notice under due process analysis, and had acted with the consent of a majority of bondholders. The court also noted

6. 374 BR 516 (SDNY 2007), aff'd, 309 Fed Appx 455 (2d Cir 2009), cert denied, 558 US 1007 (2009)

that the impairment of the bondholders' ability to collect was a result of bankruptcy law, and not the result of any act of the bond trustee; the lease could unquestionably be impaired under bankruptcy law, and the court found that the indenture trustee's power to prosecute a claim for breach under the lease inherently included the authority to compromise that claim. Accordingly, the district court affirmed the settlement order, notwithstanding provisions of the trust indenture that might otherwise have given the dissenting bondholders a blocking vote on the settlement.

Among the most important ramifications of the Delta/KCAB case, and others like it, is the clear authority found by the court under federal bankruptcy law for judges to modify the contractual terms of credit arrangements even in the face of bondholder dissent, even when the trust indenture might otherwise require the trustee to obtain unanimous or super-majority approval by bondholders, and even in the sacrosanct world of municipal finance. With many US municipalities on the verge of serious financial distress, investors in bonds and other municipal debt instruments must now consider the possibility that, 'trust arrangements' notwithstanding, a federal court has the authority to approve compromises on investor rights even when such compromises alter the terms of a trust indenture and are not acceptable to minority bondholders.

CONCLUSION

As illustrated above, the wide variety of commercial trust structures found in the US, from the traditional to hybrid forms combining elements from corporate and other business organisation structures, highlights the priority US investors place on independent fiduciary management in any context when significant sums are at stake. Although courts continue to grapple with the basis for and extent of a trustee's duties in the commercial context, it seems reasonable to conclude that the more traditional the trust structure, the more likely the commercial trust in question will be treated under the general fiduciary standards for trusts of the given jurisdiction.

Lawyers, accountants and other professionals consulting at the formation stages of these commercial trusts would do well to collaborate with colleagues well versed in the strong and weak points of trusts administered in the private sector. In US jurisdictions particularly tied to the common law (including Delaware and New York), this collaboration will facilitate a much more meaningful setting of expectations from the outset of the investment cycle, and assist all parties in assessing benefit, risk and pricing in ways that reduce the risk of contentious litigation ahead.

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Compare and contrast

Is a deed of variation executed under English and Welsh law a 'comparable legal instrument' under German inheritance and gift tax law?

By Susanne Thonemann-Micker and Jan-Lukas Lüken

Abstract

- **There are difficulties in adapting foreign legal instruments under German inheritance and gift law tax.**
- **Comparable foreign legal instruments can be subsumed under German legal instruments and accordingly recognised in German inheritance and gift tax law.**
- **The legal instruments must have the same economic results to be considered comparable.**
- **In certain cases, a deed of variation under English and Welsh law and a disclaimer of inheritance (in exchange for compensation) under German law can be regarded as comparable.**

The succession laws of Germany and England and Wales operate differently, due to the countries' different legal systems. As a result, the legal instruments and estate-planning possibilities within the respective succession regimes are not easily comparable. This raises the question of how a German inheritance and gift tax liability arising from a cross-border succession is dealt with in Germany when the law of another state applies to that succession, particularly in relation to transactions from a foreign testator/donor that are subject to foreign domestic law, to an heir/donee who is subject to unlimited taxation in Germany. One solution to this problem, we argue in this paper, is to subsume legal instruments that are unknown to German law under comparable legal instruments under German civil law so that these instruments can be recognised under German inheritance and gift law tax.

This article considers whether there are German legal instruments that are comparable to a deed of variation (DoV) executed under English and Welsh law and, if so, how a DoV would be treated under German inheritance and gift tax law.

If all legal and testamentary heirs are taken into account under the DoV, as they would be in a

disclaimer of inheritance (which means the beneficiaries of the DoV would be the advancing legal or testamentary heirs), then the two instruments may be deemed comparable. If these instruments are not deemed comparable, from a German tax point of view, the assets will not be transferred directly to the persons favoured by the DoV. In the first instance, there would be an interim acquisition by the original heir according to the last will or legal succession, which would be taxable. The transfer to the person favoured by the DoV would be seen as a gift that is taxable, too. Therefore, the DoV would lead to two taxable transactions under German tax law.

Before comparing the two instruments, we have provided a brief overview of the DoV and the disclaimer of inheritance (in exchange for compensation).

A. OVERVIEW

I. Deed of variation

English and Welsh inheritance law follows the principle of a separate administration of the estate; in the first instance, the whole estate is transferred to a personal representative. The personal representative becomes the possessor of the estate and it is their task to gather all assets of the estate and manage them for a certain time. The personal representative is also obliged to settle the debts of the estate and finally to distribute the net estate to the legal and/or testamentary heirs, or to convert it into a long-term trust. A DoV can be used by the heirs to change the testamentary disposition of the deceased with the result that the deed is to be treated as if the deceased had made the disposition themselves. Thus, the DoV can lead to tax advantages, as it makes it possible to skip a generation without having to pay additional inheritance tax (IHT).

To be effective, the DoV must be completed within two years after the death of the testator, the appropriate tax statements must be filed, and agreement must be gained from all persons whose rights are affected by the deed.

II. Disclaimer of inheritance (in exchange for compensation)

According to German succession law, the principle of universal succession applies.[1] This means that the heir(s) enter into the entire legal position of the deceased at the time of their death and directly acquire all assets and liabilities. Each heir has the option to disclaim the inheritance.[2] The disclaimer of inheritance repeals the succession retroactively and the replacing heir immediately steps into the legal position of the disclaiming heir. In return, the disclaiming heir may receive compensation. The compensation should be subject to a separate agreement between a disclaiming and replacing heir and is valid only on the condition that the inheritance is disclaimed.

According to German civil law, the disclaimer of inheritance (in exchange for compensation) is a unilateral declaration of intent that cannot be subject to a condition. In principle, the declaration has to be delivered to the probate court within six weeks after the heir receives knowledge of their status as an heir and the reason for them becoming an heir.[3] The deadline for declaring the disclaimer of inheritance can be extended to six months if the deceased's last domicile was abroad or the heir was residing abroad at the beginning of this period.[4] The principle of universal succession and the fact that the testator's will cannot be varied after their death means it is not possible to disclaim parts of the inheritance; the heir may only disclaim the inheritance as a whole.[5]

Compensation for disclaiming an inheritance is subject to IHT.[6] Under German IHT law, different tax rates and tax exemptions apply depending on the relationship of the testator to the heir. When there is a disclaimer of inheritance (in exchange for compensation), the compensation is considered to be received directly from the testator and, thus, the tax rate and tax exemptions depend on the relationship between the disclaiming heir and testator. The acquisition by the replacing heir is also subject to IHT, which is calculated according to their relationship to the testator. The compensation paid to the disclaiming heir is deducted as a liability to the estate. If the compensation exceeds the fair market value of the inheritance disclaimed, the excess part of the compensation may be considered as a gift

1. Section 1922, paragraph 1 of the German *Civil Code* (BGB)

2. Section 1942, paragraph 1, BGB
3. Sections 1944–1947, BGB
4. Section 1944, paragraph 3, BGB
5. Section 1950, BGB
6. Section 3, paragraph 2, no.4 German *Inheritance and Gift Tax Law* (ErbStG)

> **The comparison to the German legal instrument is not carried out with respect to the formal content of the foreign instrument, but with respect to the economic effect the instrument of foreign law has in the individual case**

from the replacing heir to the disclaiming heir.[7] Thus, the excess amount could be subject to gift taxation, with the tax calculated depending on the relationship between the disclaiming and the replacing heir.

B. REQUIREMENTS FOR COMPARABILITY

German IHT law provides an exhaustive catalogue of types of acquisitions that trigger IHT.[8] Transactions subject to foreign succession laws that are unknown to German law have to be examined as to their comparability with transactions under German IHT law.[9] If the foreign and German legal instruments are identical in content, the foreign legal instrument can be subsumed directly – and accordingly recognised – under the relevant rule of German inheritance and gift tax law. If there is no identical type of transaction within the catalogue of the German IHT law code, an adaptation of the legal position of the taxpayer to the structures of German inheritance and gift tax law is required.[10] Therefore, the German legal instrument that comes closest to the foreign law instrument in terms of its economic effects has to be determined. If the comparison leads to a similar instrument of German law listed within the catalogue of the German inheritance and gift tax law, the foreign legal instrument can be accorded similar treatment. The comparison is not carried out with respect to the formal content of the foreign instrument, but with respect to the economic effect the instrument of foreign law has in the individual case.

7. Section 7, paragraph 1, no.1, ErbStG
8. Sections 3 and 7, ErbStG
9. Section 1, paragraph 1 and sections 3 to 8, ErbStG
10. German Supreme Tax Court judgment of May 7, 1986 (reference number: II R 137/79)

C. COMPARING THE DEED OF VARIATION AND THE DISCLAIMER OF INHERITANCE

The DoV is a legal instrument of English and Welsh law which, in its very meaning, is unknown to German law. According to German law (as discussed above) it is not possible for the heir(s) or anyone else to disregard or change the testator's dispositions after the testator's death. Under German law, the only way to vary the distribution of the inheritance from that stipulated by the testator's will is by a disclaimer of inheritance, pursuant to which the disclaiming heir may receive compensation.[11] While the legal consequences and content of a DoV and disclaimer of inheritance differ, in some cases a disclaimer of inheritance by one or more heirs (in exchange for compensation) might lead to the same economic result as a DoV.

Differences

A rather unimportant difference is the time limit for both legal instruments. The disclaimer of inheritance (in exchange for compensation) must be declared within six weeks or six months (depending on the particular case; see above) after the heir receives knowledge of their status as an heir and of the reason for becoming an heir. The DoV, however, has to be completed within two years after the date of the testator's death – a considerably longer period of time.

This leads to the question: will the structural comparability of both instruments fail if the shorter deadline for the disclaimer of inheritance has passed by the time the DoV is concluded? However, we have to bear in mind that classification of the DoV as a disclaimer of inheritance is only carried out for tax purposes, while the validity of the DoV is determined by English and Welsh law only. The requirements for an effective DoV according to English and Welsh law cannot be replaced by German civil-law rules. Therefore, we argue that the structural comparability of both instruments cannot be denied based on their different deadlines.

11. Sections 1942 seq, BGB

> **The two legal instruments should be considered structurally comparable where the same economic result is achieved**

A major difference between the two legal instruments is that, under German law, the disclaiming heir loses their status as an heir and their complete portion of the estate is assigned (proportionately) to the replacement heir(s). In exchange for their status as an heir being revoked in favour of the replacing heir, the original heir may agree on compensation with the replacing heir. In a DoV, however, parts of the estate can be passed on to an additional heir without affecting the other parties' status as heirs of the deed. Furthermore, while the beneficiaries of a DoV can be selected without limitations, under a disclaimer of inheritance the disclaiming heir cannot choose a beneficiary. The person replacing the disclaiming heir is chosen automatically either in accordance with legal succession or by the last will of the testator (if they made provisions for a replacement of an heir).

In light of these differences, some commentators do not believe these two legal instruments are comparable. We agree with this opinion in principle, but further analysis is, we suggest, necessary.

The two legal instruments should be considered structurally comparable where the same economic result is achieved. If, for example, all legal and testamentary heirs are taken into account by the DoV, as they would be in a disclaimer of inheritance (in exchange for compensation), and provided that the exact inheritance ratio (if applicable) is respected, then the DoV has no legal outcome that economically differs in comparison to a disclaimer of inheritance, and the results of both would be equal. In our opinion, this economic result means that it is irrelevant whether the beneficiaries correlate with replacing heirs in a disclaimer of inheritance according to English and Welsh succession law or according to German succession law.

The following example illustrates a situation in which there is no difference between the economic consequences of a DoV and a disclaimer of inheritance (in exchange for compensation):

The father is British and lives in England. He dies. His only son, who is his sole heir, has a residence or habitual abode in Germany. After paying the UK taxes, the net estate consists of EUR1 million in cash and EUR4 million in real estate property situated in England. The son concludes a DoV with his only two children (the testator's grandchildren), who have a residence or habitual abode in Germany as well, by which the son receives the EUR1 million cash and the grandchildren each receive half of the real estate property.

The economic consequences of this DoV are the same as a disclaimer of inheritance of the son in exchange for compensation of EUR1 million. According to German succession law, the grandchildren would step into their father's position as heir (each with a portion of 50 per cent) in relation to the grandfather if their father disclaims the inheritance. Under both instruments, the father would keep the EUR1 million (either as his remaining inheritance according to the DoV or as compensation for disclaiming the inheritance) and the real estate property would be divided between the two grandchildren (either as beneficiaries according to the DoV or as heirs to their grandfather).

This means that, if the requirements mentioned above are met, the DoV and the disclaimer of inheritance (in exchange for compensation) are comparable in terms of their economic effect, and in such cases the DoV can be treated as a disclaimer of inheritance for German tax purposes.[12] This result corresponds with the above-mentioned criteria of comparability of economic effects developed by the German Supreme Tax Court.

12. Section 3, paragraph 2, no.4, ErbStG

D. CONCLUSION

The treatment of the DoV as a disclaimer of inheritance (in exchange for compensation) for tax purposes is not without controversy. If the DoV might trigger German IHT, the legal and tax consequences both in Germany and in England have to be examined and coordinated. It may be prudent to clarify the tax effects of the planned DoV in Germany with the local tax authorities through a ruling in order to avoid gift taxation on the transfer from the disclaiming to the replacing heir. At least the disclaiming and the replacing heir(s) should be informed about the tax consequences if comparability is denied.

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ADR and Trusts:
an international guide to arbitration and mediation of trust disputes

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By Grant M Jones and Peter Pexton; reviewed by Andrew Kidd

Grant Jones and Peter Pexton's book, *ADR and Trusts: an international guide to arbitration and mediation of trust disputes*, is a welcome addition to an uncrowded area of legal writing, written in a practical way for the busy practitioner. It will no doubt be used by those new to this area of practice and senior practitioners alike, as it is authoritative, up-to-date and full of useful information on the law and practice of arbitration and mediation.

Alternative dispute resolution (ADR) has a prominent place in the long-term debate about the future challenges that the profession faces. I can speak only as an England and Wales solicitor, but there can be no question that the legal profession generally faces radical change over the medium to long term. First, there is downward pressure on costs, coupled with the constant ways in which those who need legal services seek to reduce their expenditure. A second factor is the liberalisation of the marketplace flowing initially, in England and Wales at least, from the *Legal Services Act 2007*. Finally and, to my mind, most significantly, there is the impact of disruptive technology, whereby the computer will become not just the tool of first resort, but the only tool.

There are, of course, differing schools of thought as to how practitioners will fare in the face of these changes, but all this could mean that any area of practice that is inherently more adaptive and flexible, taking fully into account the range of issues involved (not just the legal ones), must to some extent hold long-term attraction.

Indeed, ADR must have further appeal for those embroiled in trust litigation, which can combine legal complexity with often deep-rooted family tension. Aside from the potential cost implications of not considering ADR, it should remain a popular means of resolving disputes in a contractual, non-litigious way.

“This book will no doubt be used by those new to this area of practice and senior practitioners alike, as it is authoritative, up to date and full of useful information on the law and practice of arbitration and mediation

The authors, both of whom have a truly international background, have a sound grip on their subject. The work is split into two sections, the first being dedicated to a comprehensive introduction to dispute resolution, including an overview of the benefits of mediation for trust and fiduciary disputes, and an analysis of cross-border aspects and issues.

However, practitioners will no doubt also use the work as a point of reference: the majority of the book is dedicated to thoroughly researched and well-ordered jurisdictional summaries, prepared by local practitioners. All of the main jurisdictions are covered, as well as the usual suspects, including Australia, Cyprus, Hong Kong, India and Malaysia. The names, addresses and email addresses of the local contributors are also included. This is of real assistance to the busy practitioner in need of reputable and competent counsel in a relevant foreign jurisdiction.

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