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EDITORS NOTE

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Welcome to the first edition of Private Matters, our bimonthly update to keep you informed about the issues that affect our private clients. Whatever the subject, at Mishcon we fiercely guard our clients' interests, going beyond the call of duty, making your problems our own, so that you can feel confident we will solve them quickly and professionally. This month's edition focuses on art, tax, divorce, privacy and fraud.

STOPPING THE MODERN DAY MADOFFS: RECOGNISING THE RED FLAGS

The profile of the super-rich has been transformed over the past 25 years by the emergence of oligarchs, dotcom millionaires and hedge fund managers. The significant shift from inherited to self-made wealth has left many asking… can I make that kind of money?

Modern day Madoffs are exploiting the combination of our newly formed aspirations to become self-made millionaires, our ignorance as to how such sums are actually made and the relative decline in the attraction of traditional investments. Bernard Madoff pioneered one of the most infamous Ponzi schemes, which collapsed in 2008 leaving around $65bn in losses and over 16,000 victims – none of whom were any the wiser as to the initial premise of the scheme they had been persuaded to invest in.

Now that people are wise to Ponzi schemes, new types of fraudulent investment schemes are on the rise. They rely on the same components – aspiration, misguided trust and a lack of understanding. The latest schemes purport to involve bank instruments, medium term notes (MTNs) and government bonds. The fraudsters claim to have access to secret trading platforms and private placements. The exclusive schemes they present are said to be sanctioned by organisations such as the Federal Reserve, the World Bank or the IMF. They are available only to an elite – flattery can still get you somewhere. The deal: you invest several millions (from £2 million to £200 million) and you are guaranteed almost immediate, massive, risk-free returns.

There will be a big player behind the scenes, who you will not be allowed to meet, and over months or even years, your credentials will be checked by a core group or 'team' of individuals who you know and trust. You will not be allowed to forget the privileged position you are in. Once you are finally accepted onto the scheme, you will be instructed to transfer your funds to a "blocked account" so that it is ready "to be traded". You remain confident that your funds are secure – safe in the knowledge that your authority is required to move them.

Once in this "blocked" account your funds will either be transferred without authority - a straightforward theft. Alternatively the, by then trusted, team will explain that there are unexpected last minute problems, matters beyond their control, and the funds must be transferred to another account; they will only be out of your control for a matter of days. Once they have control over the funds, they are quickly dissipated across numerous jurisdictions. By the time you realise what has happened your money is long gone, transferred across the globe. The team no longer respond to emails or calls; you have no other way to contact them and realise no legitimate business address was ever provided to you.

It's embarrassing. Often with hindsight the team are seen for what they are - fraudsters. The reason you couldn't find them on the internet (because you looked – you tried to carry out your own due diligence) is that they aren't who they say they are; they didn't live the luxury lifestyle they presented. You weren't invited to their office – because they never had one. You trusted these people and they've manipulated and exploited you - the last thing you would want is to publicise it.

The silver lining here is that there are red flags which you can look out for, and if you are unfortunate enough to be scammed by these sophisticated fraudsters then with decisive action, investigation and injunctive intervention, it is possible to recover funds and bring the fraudster to justice – in both the civil and criminal courts.

Fraudulent investments – five red flags:

1. Secrecy
2. Stressing that you are in a privileged position
3. Excessive use of technical terminology
4. Resistance to questions
5. Last minute requirements

For more information, please contact Victoria Pigott, Associate.

GOOGLE IS WATCHING YOU: CHANGES TO GMAIL TERMS GIVE RISE TO PRIVACY CONCERNS

Recently announced changes to the Google terms of service clarify that all incoming and outgoing emails to and from Gmail accounts are analysed by software. Google now clearly specifies that all emails sent to Gmail accounts, even if you don't use Gmail yourself, will be scanned. Over 425 million people use Gmail around the world. Millions more write to Gmail addresses from Hotmail, Yahoo or other email services.

Privacy experts are concerned about the implications of the changes. Last year in a class action lawsuit filed by Google users in the US, Google was accused of breaking US wire-tapping (telephone hacking) laws when it scans emails to target ads. Lawyers were surprised when Google said in a court filing that people sending email to Gmail had no "reasonable expectation" that their communications are confidential. This coincided with the revelation that Google had provided information to the National Security Agency on US citizens and foreign nationals.

Part of Google's defence in the wire-tapping claim is that sending an email is like sending a letter via the post office: "Just as a sender of a letter to a business colleague cannot be surprised that the recipient's assistant opens the letter, people who use web-based email today cannot be surprised if their communications are processed by the recipient's ECS (electronic communications service) provider in the course of delivery".

But the claimants argue that sending an email is very different to sending a business letter. Most people do expect their emails to be private. They don't expect a virtual personal assistant or secretary to be opening their email. They especially don't expect it when they're communicating about medical issues, their children, or aspects of their lives that they wouldn't necessarily put in a business letter which might be opened by a secretary.

Kate Wilson, a barrister at One Brick Court chambers, who specialises in media and information law said:

"People who have signed up to Gmail may have agreed to this, but those sending emails to a Gmail account user have not. They haven't consented to the use of their information. There are serious privacy implications for non-Gmail users, in particular if Google can relate the information obtained from scanning emails to the sender of the email, by way of IP address or other identification from the sender's email address. "

In other words, Google may be able to work out who has written the email – and may then be holding data on individuals which potentially infringes European data protection laws. In the light of the Google Spain judgment, this may complicate their position even further.

"This practice may lead to claims by non-Gmail users for misuse of private information and breaches of data protection laws" added Ms. Wilson.

Of course, Google is also collecting data from your YouTube browsing, your map searches and your Google searches themselves. Industry insiders say that everyone using Google services knows the score.

"You don't pay for these services, so ads have to be targeted in some way. One thing we know is that people don't want to pay for services, and are willing to have their information tracked in order to avoid paying" says one digital media director.

As Google put it:

"Our automated systems analyse your content (including emails) to provide personally relevant product features such as customised search results, tailored advertising and spam and malware protection".

Federal District Judge Lucy Koh in San Jose, California has already rejected Google's attempt to dismiss the wire-tapping case by rejecting its argument that users agreed to scanning when they accepted its terms and conditions.

The Google lawsuit in the US combines several claims from 2010 – 2012 by Gmail users and email services in states including Texas, Pennsylvania and Florida. It also includes people who have used Google's apps for education. It appears that Google used the technology to extract information from unopened, deleted or emails which were accessed by mobile phones. This technology, the claimants argue, is equivalent to hacking into your emails.

Google's changes to its Ts and Cs matters. Not just because the company is in the middle of a contentious lawsuit, but because it dominates online searches. Anyone using a Google service – which is almost everyone who goes online – must understand what they've signed up for. And anyone who hasn't signed up for a Google service must understand what is going to happen to private communications sent to Gmail addresses.

For more information please contact Dina Shiloh, Solicitor.

NAVIGATING THE LEGAL MINEFIELD OF DIVORCE IN THE US VERSUS DIVORCE IN THE UK

New figures show over three-quarters of those who use London's commercial court to settle disputes are from outside the UK. The figures, from Portland Legal Disputes, identified the nationalities of the parties in 141 High Court rulings between April 2013 and March 2014. Where a case is litigated can significantly influence the outcome and divorce is no exception.

Between 40 and 50 per cent of marriages in the US and England end in divorce and for transatlantic economic migrants there is one added layer of complication: where to divorce, their country of origin or their country of residence? The US and England's respective divorce regimes are often more favourable to one spouse than the other, which can prove to be a legal minefield.

In the US financial claims are determined on the basis of 'equitable distribution' or 'community property'. Most States have equitable distribution laws. What this means is that, on divorce, marital property will be divided between the spouses in a fair and equitable manner and separate property (anything generated prior to the marriage or received as a gift from someone other than one's spouse or inherited during it) is not susceptible to division. There is no set rule to determine who receives what or how much.

Nine States, including California, have the community property regime which means spouses are deemed to equally own all income earned and assets acquired during the marriage, irrespective of who earned the income or bought the assets. All income is shared equally and all community debts are similarly divided.

English law falls somewhere between the two. Marital assets are shared broadly equally between the spouses on divorce. However, if the division of marital assets does not sufficiently meet the needs of the parties, the court can order the transfer of non-marital assets by one spouse to the other. Furthermore, where one spouse has given up a career to raise the couple's children, the court can order the transfer of assets as compensation.

Whether it's possible to issue proceedings in England or the US depends on the relevant court having jurisdiction over the marriage and its dissolution. Divorce in the US is State governed and they each have their own residence requirements which govern whether courts have jurisdiction to deal with divorce. Under New York law, for example, residency periods vary and can be for as long as two years depending on circumstances. "Residency" however, does not require full-time presence in the State. Meanwhile, in California, one of the parties to the marriage must be resident in the State for six months before the divorce petition is filed. Under English law, various routes are available to resident, non-domiciled, individuals who wish to issue divorce proceedings.

And if this isn't complicated enough, careful thought must also be given to the US tax consequences of the transfer of assets or payment of maintenance on divorce, whether in relation to US or English income and assets.

For more information, please contact David Lister, London and Michael Stutman, New York

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THE DEFINITION OF ART HAS ONCE AGAIN BECOME TAXING

Due to materials often used, tax and contemporary art have not always sat well together, particularly in relation to customs law and VAT.

The latest twist in the relationship between tax and the definition of art involves the recent case of *The Commissioners of Her Majesty's Revenue and Customs v The Executors of Lord Howard of Henderskelfe* (Deceased) [2014] EWCA Civ 278, ('Omai'). The artwork at the centre of the dispute is oil on canvas, "The Portrait of Omai" painted by Joshua Reynolds (the 'Painting'). The financial and intrinsic value of the Painting was acknowledged at auction in 2001 when it sold for a world record amount for a painting by Reynolds.

The central issue of the Omai case was whether the executors were chargeable for capital gains tax ('CGT') on the gain made on the sale of the Painting. The dispute focused on the legal definitions of "plant" [a fixed asset] and "a wasting asset" under the Taxation of Chargeable Gains Act 1992 ('TCGA'). The matter heard before LJ Rimer, LJ McCombe LJ Briggs in the Court of Appeal had previously been heard in the upper tribunal (Tax and Chancery Chamber) [2013] UKUT 0129 (TCC) on appeal from the first-tier tribunal [2011] UKFTT 493 (TC).

History

Lord Howard of Henderskelfe owned the Painting between 1796 and his death in 1984, during which time he lent it to Castle Howard Estate Limited ('CHEL') for display at Castle Howard, which has operated as a historic open house since 1952. It remained there throughout the season and visitors were charged an admission fee.

No fee was paid to Lord Howard for the artworks on display and, on his death, the arrangement continued between the Executors of the Lord Howard and the Trustees of CHEL. There was no distinction between the Executors and the Trustees as they were composed of the same individuals. The Painting was conditionally exempted from inheritance tax - it was primarily kept in the UK and seen by the public. The Painting remained on public display between November 1984 and November 2001.

The Executors of Lord Howard's will had the power to license CHEL to use any of the chattels forming part of the Estate. The Painting was put up for sale in 2001 and it had a hammer price of £9.4m, from which commission and VAT totalling £220,900 was deducted. This sale price represented a substantial gain over the value of the Painting at the time of Lord Howard's death. (It has subsequently been reported that the Painting was sold onto a private buyer for £11.6 million.)

The Executors submitted a tax return on 29 January 2003, including the gain made on the disposal of the Painting as a chargeable gain. In June 2003 the Executors amended their tax return on the basis that the gain achieved on the sale of the Painting was exempt from CGT by virtue of Section 45 of the TCGA. They stated that the sale constituted disposal of a plant and under Section 44 (1) (c) of the TCGA the Painting was a wasting asset.

HMRC rejected that the gain was exempted by Section 45 of the TCGA and they rejected that the Painting was plant. They subsequently issued a closure notice on this basis. The Executors appealed against this closure notice on 28 May 2010 and the Reviewing Officer upheld the HMRC's closure notice in full on 5 August 2010. At the first tier tribunal hearing, HMRC's position in 2011 was upheld, however, at the upper tier tribunal in 2013, the appellants - the Executors - were successful and this decision was supported at the Court of Appeal this year.

According to HMRC, not every chattel is automatically 'plant' and it was possible for a chattel to have varied 'personalities' depending on who held them. They held that the Painting was not 'plant' in the hands of the disposing party and therefore no CGT exemption under the TCGA applied. Also, to be a wasting asset, it had to be a wasting asset in the hands of the person disposing of it (and the Painting was not in the hands of the Executors).

HMRC stated that the Painting was not integral to the historic house business and visitor numbers had actually increased since it was removed. The Painting was not a business asset of CHEL and CHEL were not the disposing party. There was a concern that potential tax avoidance issues may arise if it was possible for an asset to qualify as plant, even if it was a privately owned asset not used as a business asset by its owner that had been lent on an informal basis to a trader for free.

The Court of Appeal dismissed HMRC's appeal on the grounds that the CGT exemption under the TCGA is focused not on the identity of those disposing of the item but on the chattel being disposed. CHEL had sufficient interest in the Painting for it to qualify as 'plant' and An Old Master, worth £9.4m on its 226th birthday, once identified as 'plant' can qualify as a wasting asset under Section 44 (1) (c) TCGA.

We are not aware of an appeal to the Supreme Court by HMRC, nor is it known if new legislation may be brought in. Until then, it is worth considering:

- If you are a collector that lends or you are part of a Historic House business, are the terms of any such agreement formalised?
- Do you have artworks, antiques and collectibles on display which are central to the core of a historic house business or are they peripheral attractions? (e.g do the works feature in guidebooks?)
- Following the Court of Appeal decision, is there an opportunity to make a Potentially Exempt Transfer of valuable chattels without considerable CGT implications?
- Have you made a recent disposal that could be exempt from CGT? Are you within time to reopen the CGT assessment?

To discuss how we may be able to assist please contact Karen Sanig (Head of Art Law) or Andrew Goldstone (Head of Tax).

JIMMY SAVILE ESTATE: REMOVAL OF EXECUTORS AND THE COSTS IMPLICATIONS OF FAILING TO BE NEUTRAL

This month saw the expiry of the requested period for those claiming to have been sexually abused by the late Jimmy Savile to apply for compensation following adverts placed in national and local newspapers. The compensation scheme ("the Scheme") was established earlier this year following agreement between the executors of Savile's estate, National Westminster bank ("the Bank"), and solicitors representing the personal injury claimants. This followed a hearing where the Bank's removal as Executor of Savile's estate was sought (National Westminster Bank Plc –v- Lucas & ors [2014] EWHC 1683(Ch)).

Savile died in October 2011 and by his Will he appointed the Bank as his executors. The beneficiaries of his Will included his niece and the Jimmy Savile Charitable Trust ("the Trust"). In March this year, his estate was valued at around £3.3million. The information regarding Savile's actions, which came to light after his death, is well documented and followed an ITV documentary in October 2012, which accused Savile of being a serial child abuser and sex offender. By March 2014, 139 people had intimated personal injury claims to the Bank on the basis of being abused by Savile. There were also potential claims against third parties (including the BBC, certain NHS hospital trusts and the charities Barnardo's and Mind) that would have claims against the estate for an indemnity. If such claims, as yet untested, were found to have merit, the entire estate could be exhausted leaving little, if anything, to be distributed to the named beneficiaries and a possible insolvent estate.

In March, the Trust applied to remove the Bank as executor and their replacement with an alternative professional executor, PennTrust Limited, to act as personal representative. The Trust's application for removal of the Bank was dismissed. The Bank's application for approval of the Scheme was successful.

Broadly, when seeking to remove an executor, the claimant party must establish that it will be in the best interests of the beneficiaries for the executor to be removed. It is not necessary to show any deliberate misconduct or a breach of trust by the executor, a breakdown in relations may be sufficient, however this is not a guarantee of success and in this case, this ground did not succeed for the Trust.

The Trust put forward nine grounds seeking the Bank's removal and failed on every ground. These included allegations that the Bank had not included the Trust in all its meetings to agree the terms of the Scheme and preferred the interests of the personal injury claimants (the Bank was found to have acted in an entirely proper manner); the Bank had acted with hostility (it was noted that there are contexts in which a personal representative has to make judgements which involve striking a balance between competing interests and there will often be an element of friction); the Bank had agreed to retire but did not follow through with this (it was noted that there was no final agreement to retire and it had good reasons not to, as progress had been made on negotiating the Scheme) and that the Bank had improperly shared confidential information with the personal injury claimants (also rejected).

In his Judgment, Mr Justice Sales referred to the principal nineteenth century authority on the removal of an executor or personal representative, Letterstedt -v- Broers (1884) 9 App Cas 371, which was applied in the 2007 case of Thomas and Agnes Carvel Foundation -v- Carvel [2007] EWHC 1314 (Ch), noting that the overriding consideration is whether the trusts are being properly executed and the broad principle of the welfare of the beneficiaries is to be applied with reference to the particular circumstances of the case. Clearly, friction and hostility are not enough to remove a professional executor.

Further, at a costs hearing in April (National Westminster Bank -v- Lucas and others [2014] EWHC 1683 (Ch)), having lost the earlier removal application, the Trust found itself on the receiving end of an order to pay the costs of the Bank, the personal injury claimants and some of the other parties (totalling over £200,000) on what is known as the 'indemnity basis' (i.e. costs which are penal in nature, at a much higher level than the 'standard basis' and there is no requirement for the costs to be proportionate). It was found to have "adopted an unreasonable and misconceived stance", particularly having lost on every point – a clear warning to a beneficiary who might consider applying to remove an Executor, especially in a potentially insolvent estate such as this.

The Trust's actions served to increase the costs of the administration. Had the application merely been one for guidance or to address a question in the administration, costs might have been paid by the estate (see Re Buckton [1907] 2 Ch 406), but as the Trust had made the application adversarial, it had therefore put itself at risk. This is particularly dangerous for a charity that would need to call on charitable funds to meet the costs.

It is understood that the Trust is planning to appeal the costs decision. We will watch with interest the outcome of that appeal.

For more information, please contact Bethan Byrne, Professional Support Lawyer.