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In the Courts 2015: Trusts and Estates

Petitions: standing and requirements of petitioners

Trustees' powers and discretions

The manner in which trustees should exercise the discretion conferred on them, particularly as regards the payment of taxes, and the extent to which it is permissible for them to seek approval from the Court were among the issues in a significant case in Bermuda, *In the Matter of ABC Trusts* [2015] SC (Bda) 29 Civ (10 September 2014). This was a contested application by the Trustees for further directions in relation to broader approval sought for a momentous decision, and raised legal questions which the Court felt were likely to be relevant in future cases.

The decision in question involved the conclusion of negotiations that had been ongoing for some years with onshore tax authorities about certain personal 'wealth' taxes which were potentially due from the Trusts and/or the beneficiaries. It was approved by the Court on 18 August 2014 and supported by all but one beneficiary (the 5th Defendant).

Despite arguments to the contrary by the 5th Defendant, the Court determined that the Trustees had not, in seeking directions, surrendered their discretion to the Court, merely that the decision was so momentous that it sought the blessing of the court for the action.

Further, and perhaps more importantly, the Court considered whether the Trustee was required to have regard to the wider social effects of the proposed settlement and to interests other than those of the beneficiaries. In the context it was argued that paying a fair amount of tax was more in the interests of beneficiaries than paying the minimum possible, thus the Trustees were under an obligation to ensure the terms of the proposed tax settlement were demonstrably fair from a community perspective, as opposed to from a trust/beneficiary perspective. Whilst no legal authorities were cited by the 5th Defendant, numerous commentaries were discussed.

The Court ultimately sided with the Trustees' submissions (relying on *Speight v. Gaunt* (1883) 22 Ch D 727 at 739) that a "*trustee ought to conduct the business of the trust in the same manner that an ordinary prudent man of business would conduct his own.*" Judicial notice was taken that ordinary prudent businessmen seek to minimize business expenses, be they tax obligations or otherwise, and seek to enhance rather than diminish the value of their own assets.

It was therefore found that it would be an unreasonable way of expending trust assets to investigate the need to pay a further premium to ward off the risk of wholly unjustified criticism of a tax settlement which was manifestly hard fought and negotiated on objectively credible terms, and in circumstances where there appeared to be no obvious inequality of arms between the parties. The Court deemed the Trustees' decision to be consistent with the best interests of the Trusts and their beneficiaries as a whole.

In the British Virgin Islands, the exercise, in the context of contentious family proceedings, of a power contained within a trust instrument to exclude the settlor and his remoter issue as a beneficiary of the trust came before the Court of Appeal in *Royal Fiduciary Group Limited (Re The New Huerto Trust)* BVIHCMAPP 2013/0022, 26 October 2015, unreported. Bannister J refused to sanction the exclusion, declining to follow the English decision in *Blausten v. IRC* [1971] 1 WLR 1696 which he described as 'obviously wrong'. The Court of Appeal held that it could see no reason, based on principle, why the trustee could not properly exercise the power of appointment conferred on him, by excluding the settlor from benefiting under the trust.

In a series of decisions all relating to the same set of trusts, the Royal Court in Jersey has given guidance to trustees as to the proper exercise of their discretions when a trust is considered insolvent. Whilst it is of course the case, as the Court itself has observed, that a trust cannot itself be insolvent, the concept of an insolvent trust is a useful shorthand in dealing with a structure where the liabilities exceed the assets of the trust. Such a phenomenon is possible in jurisdictions such as Jersey, where as a matter of law a trustee cannot be personally liable to a third party for an amount greater than the assets of the trust.

Representation of the Z Trusts [2015] JRC 214, [2015] JRC 196C and [2015] JRC 031 addressed various issues arising in the context of trusts whose liabilities vastly exceeded their assets. In particular, the Court held that the trusts should be administered under the direction of the Court, and that the interests of the creditors were to be regarded as paramount. If no solution could be found by which the trusts could be restored to solvency, it would be appropriate for the trusts to be subject to a 'winding up procedure', under which the assets of the trusts would be liquidated and distributed to creditors on a pro rata basis. Unless disabled from acting by a conflict of interest, it would be appropriate for the trustee to rule on the validity of creditor claims (which would be submitted in the form of a proof of debt) and to oversee the distribution of the assets.

The Court also set aside an attempt by the Settlor of the trusts, who retained a power to remove and appoint new trustees, to remove and replace the trustees of some of the trusts. It held that in this context, the power holder owed a fiduciary duty to all of the creditors as a class, rather than to the beneficiaries, and the power could not accordingly be properly exercised unless it was exercised in the interests of all of the creditors. The fact that a majority of the creditors had supported the exercise of the power was not sufficient.

The Court further confirmed (in reliance on the recent *Glenalla* decision in Guernsey (Judgment 41/2014, 29 October 2014, unreported)) that a former trustee of a trust is entitled to exercise a common law lien over the trust property in order to satisfy liabilities arising out of its trusteeship of the trust. For further detail on this aspect in particular, see our eAlert on the case.

A further case from Jersey regarding court approval of trustee decisions provides interesting observations as to the extent of the evidence required in support of such applications and the nature of the test on appeal. *Representation of Otto Poon Trust* [2015] JCA 109 (20 May 2015) concerned an appeal from the Royal Court's decision to bless a trustee's decision. At first instance the Royal Court indicated that the trustee's affidavit in support of its application for a blessing of the trustee's decision 'could have been fuller' as to the reasons for its

decision, but unusually accepted as evidence further explanations from the trustee's advocate as set out in the trustee's skeleton argument.

The Court of Appeal went further than the Royal Court, describing the affidavit evidence of the trustees as 'inadequate' and indicating that in other circumstances it could have been held to be insufficient, resulting in a rejection of the trustee's application. It, however, rejected the contention that it was now a requirement in such cases for trustees to set out in detail the steps taken in their decision making process. The Court indicated that each case would turn on its own circumstances and facts. Where the trustee's decision is a difficult or complex one requiring a fine and delicate judgment and the weighing up of conflicting considerations, the Court observed that the quality and nature of the decision making process will be of far greater importance than in cases where the decision is relatively straightforward, albeit momentous. The Court of Appeal, whilst blessing the trustee's decision on this occasion, nevertheless stressed that trustees should certainly not take a casual approach to applications of this nature, and it is clear that careful thought will need to continue to be given to the filing of comprehensive evidence in most cases.

As to the nature of the test on appeal in relation to such applications, the Court of Appeal stressed that it was not helpful to apply the usual test in relation to appeals against the exercise of discretion of the Royal Court. The question before a Court of Appeal in such applications was essentially identical to the question before the Court below; namely to review the rationality of the trustee's decision on the evidence and not the rationality of the Royal Court's assessment. Thus the Jersey Courts, following the Guernsey case of *Re F* (Court of Appeal, Judgment 32/2013, 10 September 2013, unreported), have effectively determined that appeals in this area amount to a *de novo* review of the rationality of a trustee's decision.

***Hastings-Bass, Pitt v. Holt* and Trustee Mistake**

By the enactment of the Trustee Amendment Act 2014, the Bermuda legislature inserted a new section to 47A into the Trustee Act 1975. The purpose of this reform was to introduce the 'Rule in *Re Hastings-Bass*' as it had been understood in England and Wales (and other common law jurisdictions) before the decision of the UK Supreme Court in *Pitt v. Holt* [2013] 2 AC 108, and to provide a statutory mechanism by which flawed decisions of trustees and other fiduciaries could be set aside upon application to the court. (Jersey has followed a similar approach).

The cases of *In the Matter of F Trust* and *In the Matter of A Settlement* ([2015] SC (Bda) 77 Civ (13 November 2015)) are the first to receive judgment under the new provision. The decision related to two Bermuda trusts in each of which a UK resident trustee had been appointed. Holding that section 47A (1) confers an unfettered discretion upon the Court to grant relief provided the threshold requirements are met, and accepting in each case that there had been a failure to take into consideration the significant UK tax consequences of such appointments, the Court set aside the flawed exercise of powers of appointment. The decision is discussed in an Appleby eAlert.

In Guernsey, unlike Jersey and Bermuda, the matter has not been the subject of legislation. However, the Royal Court has held, in the first case where the so-called rule in Hastings Bass was in issue, that a form of the rule does form part of Guernsey law: *In the matter of HCS Trustees Limited and another v. Camperio Legal and Fiduciary Services Plc and another* (unreported). The Court did not comment upon the precise ambit of the rule. Under English law, the application of the rule in Hastings-Bass has been significantly tightened and applicants now have to establish that trustees' inadequate deliberations have been sufficiently serious as to amount to a breach of fiduciary duty. Until the precise ambit of the rule under Guernsey law has been

determined, the question remains open as to whether a more lenient test for relief may apply under Guernsey law: namely, one that does not require breach of a fiduciary duty. The Guernsey decision is discussed further in Appleby's eAlert on the subject.

In *Schroder Cayman Bank and Trust Company Limited v. Schroder Trust A.G.* (Grand Court, FSD 112/2014, 9 March 2015, unreported) the Chief Justice considered the test for mistake as set out by the UK Supreme Court in *Pitt v. Holt* [2013] 2 AC 108 but did not have to decide whether its limitation of equitable relief for mistake to cases of genuine mistake where it would be unconscionable to refuse relief, fell to be applied in the law of the Cayman Islands. The case concerned three separate appointments of capital from an employee benefit trust established in the Cayman Islands to three employee financed retirement benefit schemes in Jersey. The appointments were made on the basis of erroneous advice from English solicitors that they would not trigger an Inheritance Tax liability and that they were permissible under the powers contained in the Cayman trust. On the facts, the Court held that the appointments were void as a result of an excessive execution of powers contained in the relevant Trust deed by the Trustees on the grounds of mistake. Alternatively, the Court held, the mistake was in any event so fundamental that the case fell within that category of case where even on the narrower approach set out in *Pitt v. Holt*, relief should be granted.

In separate proceedings in Jersey (see discussion re "firewall provisions" below), the Jersey Court granted recognition of the decision of the Cayman Islands court such that the Trustees will be entitled to rely on that decision in any subsequent proceedings brought in Jersey in connection with the employee financed retirement benefit schemes. For more detail, see our eAlert on the case.

A further aspect of the *Pitt v. Holt* decision came up early in the year in a case in Guernsey, *In the matter of BiGDUG Limited Remuneration Trust* (Judgment 01/2015, 15 January 2015, unreported). In *Pitt v. Holt*, Lord Walker suggested that, even in cases where the other aspects of the test set out in that case were satisfied, relief might nonetheless be refused on public policy grounds, such as in a case involving aggressive tax avoidance.

On the facts, although the Royal Court had jurisdiction because the trustee was a Guernsey trust company, the matter fell to be decided under English law, so the case does not decide where Guernsey law stands on the Hastings Bass/Pitt v. Holt issue. But in considering whether relief should be refused on the tax avoidance point, the court noted that there was no suggestion that the transaction was in any way unlawful, and proceeded to grant relief. The case is the subject of an eAlert, available here.

Protectors

An important case involving removal of trustees and protectors was decided in Jersey in September. *In the matter of Jasmine Trustees and the Piedmont Trust* [2015] JRC 196 (23 September 2015) is unusual in that the appointment of trustees and protectors were declared invalid and the fiduciaries were thus effectively removed from office on this basis rather than as a result of conduct whilst in office.

In brief, the case involved two family trusts in circumstances where the father as protector purported to appoint new trustees and then purported to appoint his sons as protectors of one of the trusts. At the same point the majority of the adult beneficiaries (including the father, the sons and the adult children of the sons) appointed the sons protectors in relation to the second trust. Those appointments were challenged by the daughter beneficiary who was estranged from her father.

The Court confirmed that a person (whether trustee, protector or some other person with a power of appointment, including a beneficiary) is exercising a fiduciary power in relation to any appointment. As such the person exercising that fiduciary power is obliged to act reasonably, in good faith and in the interests of the beneficiaries as a whole, taking into account only relevant matters.

The Court concluded that the father in appointing the new trustees had failed to take into account relevant factors such as the experience, expertise and financial standing of the proposed new trustees and had thus reached a decision that no reasonable appointer could have reached.

In addition, the Court declared invalid the appointments of the sons as protectors by reason of a significant conflict of interest between the sons and the daughter making it impossible for them to act fairly as protector (for her and others), and because the history of the matter had, upon proper analysis, revealed that the sons had not over a number of years acted independently from their father but had simply complied with his wishes often to the detriment of the daughter. The Court found as a further and additional factor that if the sons were appointed protectors, the historical and current hostility and suspicion between the various members of the family would inevitably lead to a frequent involvement by the Court as to the administration of the trusts, thus making the administration wholly impracticable. For more detailed commentary, see our article and eAlert on the case.

In Guernsey, the Royal Court was also faced with an application to remove a protector. Applying an earlier decision of the Jersey Court, the court set out the principles applicable to the removal of a Protector of a Guernsey law trust. This case, *In the matter of K Trust* (Judgment 31/2015, 14 July 2015, unreported), concerned a discretionary settlement, which was referred to as 'the K Trust.' The application was brought by 11 of the 14 adult beneficiaries of the K Trust, requesting that the protector of the K Trust be removed with immediate effect. The beneficiaries had lost trust and confidence in the protector following a breakdown in relations between the protector and the settlor's wife, rendering the trust 'unworkable,' as most of the powers of the trustees required the protector's consent. The Courts, it held, will ultimately be guided by considerations over the welfare of the beneficiaries and the competent administration of the trust in their favour. Where a breakdown in relations has a significantly detrimental effect on the execution of the trusts and is likely to continue to do so, that would be a sufficient basis for the Court to exercise its discretion. It is not necessary that the protector bears the bulk of the responsibility for the breakdown in relations and the consequent difficulties caused for the trust, but such a situation will serve to fortify the conclusion that it is right for the protector to be removed.

Application of foreign law: 'firewall' provisions

Three cases raised issues in relation to so-called 'firewall' provisions – those provisions in a jurisdiction's trust laws that assert exclusive jurisdiction over certain trust issues and exclude the application of foreign law.

In the BVI, in *Lucita Angeleve Walton et al. v. Leonard George De La Haye* BVIHCVAP 2014/004, 14 August 2015, unreported, an issue arose in relation to the firewall provisions in Section 83A of the BVI's Trustee Act. The Claimant obtained judgment in Jersey against Mrs Walton in respect of 'advances' which were to be brought back into account in settling the estate of her late mother. The Defendant alleged that Section 83A (19) operated to prevent enforcement of foreign judgments concerning heirship as being contrary to public policy. The Court held that this applied only to the extent that the foreign judgment was inconsistent with Sections 83A (13) to (18), and then where there is a disposition in relation to a BVI trust so that the BVI

legislation takes precedence over the foreign legislation. The Court held that only one such payment fell foul of these provisions. It then considered whether this was severable and concluded that it was.

The *Schroder* case in Cayman, mentioned above in the context of mistake, also illustrated an interesting clash between the 'firewall' provisions of Cayman and Jersey law. Cayman law provides that any question as to the validity of an exercise of discretion by trustees of a Cayman trust is solely a matter of Cayman law. Jersey law provides that any question as to the validity of a transfer into a Jersey trust is solely a matter of Jersey law. In a case such as *Schroder*, where Cayman trustees make a transfer into a Jersey trust, these provisions obviously collide. In the Cayman Islands case, the Chief Justice resolved the conflict by applying traditional conflict of law principles and applying the system of law most closely connected with the challenged transactions, which was clearly Cayman law.

An application to the Royal Court of Jersey was then necessitated by the fact that the assets remained held subject to the Jersey trusts. In *Representation of Schroder Cayman Bank Trust Company Limited* [2015] JRC 125, 10 June 2015, unreported, the Jersey Court noted that in ordinary circumstances it would have been required by Jersey's firewall legislation to apply Jersey law in determining whether or not the appointments were valid, which might conceivably lead to a different outcome. However, Jersey's firewall legislation had been amended in 2012 to exclude situations where there is an express provision to the contrary in the terms of the trust or disposition. That requirement was satisfied here, and accordingly the Court was in a position to give effect to the decision of the Cayman court by granting recognition to the judgment of the Grand Court. The Court however made clear that only an express provision to the effect that foreign rather than Jersey law should apply will suffice for these purposes.

Rights of Beneficiaries

The Jersey case of *Representation of X Trustees Limited* [2015] JRC 136, 23 June 2015, unreported concerned the approval of a trust variation on behalf of minor and unborn beneficiaries. The Jersey Court considered the scope of Article 47 of the Trusts (Jersey) Law, under which the Court has the power to approve a variation to the terms of the trust on behalf of the minor and unborn beneficiaries, where all of the adult beneficiaries also agree to the variation. Under the terms of Article 47, the variations must appear to the Court to be for the 'benefit' of those on behalf of whom approval is sought. The Court held that benefit in this context is to be widely construed, and is not restricted to financial benefit. In this instance, it was for the benefit of the minor and unborn beneficiaries for the trust assets to be maintained outside the scope of UK tax (which could be achieved by extending the trust period), and also for the restrictions in the terms of the trust in relation to the accumulation of income to be relaxed so that the trustee could more effectively control the flow of income in a planned way.

In the previous issue of this report we commented on a decision of the Grand Court of the Cayman Islands in a case involving a claim by the son of an intestate deceased person to enforce rights under statutory trusts. The decision of Foster, J. was overturned by the Court of appeal in *Hinds (Phillip) v. Hinds (Clive) and others* (Cause CICA 6/2013).

The facts in brief were that the husband died intestate in 1978 and, until her death in 2010, the wife dealt with certain of his real estate in Cayman as though she were the sole beneficial owner, transferring and selling certain parcels to various family members, even though the child of the marriage (the Son) was entitled by statute to a share of the husband's estate. Some parcels of land (the Retained Parcels) were still held by her at the time of her death. The Son brought proceedings shortly after the wife's death claiming that certain

properties were not part of his mother's estate, but were held for him on the statutory trusts arising on his father's intestacy.

In judgments delivered on 9 July 2014 and 5 December 2014, Foster, J. dismissed all of the Son's claims and ordered him to pay costs on the indemnity basis. Issues of standing, limitation and acquiescence all went against the Son. He appealed.

On the issue of standing, the Court of Appeal held that the judge was wrong to hold that administration could not be complete until all the assets had been sold. The ordinary rule is that administration is complete when all debts and expenses have been discharged and the residue has been ascertained. At that point the personal representative becomes a trustee in the true sense of the assets for those entitled to them. The Court was of the view that it was probable that the wife had completed administration of the estate – in the sense of discharging the debts and expenses and ascertaining the residue – well before she died. Further, even if the administration of the estate had not been completed, the Son should not be denied declaratory relief.

On the particular facts, the Court of Appeal found that the cause of action in respect to the Retained Parcels did not arise until the wife died and her administrator asserted that the properties were part of her estate. The Son's action was brought well within time thereafter.

Acquiescence and laches come into play only when a right has been infringed, since otherwise there is nothing in which to acquiesce and no right capable of being lost by delay. Further, there was no finding of any detrimental reliance by any other persons in relation to the Retained Parcels.

Interpretation of wills and trust documents

Two cases from Jersey this year have highlighted the unique position of the Crown Dependencies of Jersey, Guernsey and the Isle of Man and the fact that they are not part of the United Kingdom. The first case was *In the matter of the Estate of Meena Krishnan (deceased)* [2015] JRC 181, 01 September 2015, unreported. *Krishnan* involved a deceased who had lived much of her life in Hong Kong and was domiciled there. At the date of her death, the deceased owned two flats in Hong Kong together with various bank accounts in Hong Kong. She also held three bank accounts in Jersey together with a bond in the Isle of Man. She owned no assets in the United Kingdom as technically defined (i.e. Great Britain and Northern Ireland) but left a will referring to her 'real and personal estate situated in Hong Kong and the United Kingdom.' The difficulty arose because neither Jersey nor the Isle of Man is, as a matter of law, part of the United Kingdom, (and thus the testatrix had arguably died intestate as to her Jersey estate). However, the Court considered that this was '*not always understood by those not familiar with the constitutional niceties of the United Kingdom and its dependencies*.' The Court observed that many people mistakenly think that the Channel Islands and the Isle of Man form part of the United Kingdom, and having considered the evidence and previous authorities the Royal Court granted the order sought by the Executrix and ordered the will be admitted to Jersey probate.

The subsequent case of *In the matter of Bhasin* [2015] JRC 187, 10 September 2015, unreported, adopted the reasoning in *Krishnan*.

Tracing / Constructive trusts

The Privy Council has given cautious approval to the concept known as 'backwards tracing'. This operates in certain cases of fraud or breach of fiduciary duty, where the victims seek to trace and recover the proceeds of

the fraud or breach, but where no direct connection can be established between the funds lost by them and the funds or other assets which are found in the hands of the perpetrators.

In *Republic of Brazil et al v Durant and Another* [2015] UKPC 35 (on appeal from the Jersey Court of Appeal), the Plaintiffs were seeking to trace into funds held in Jersey bank accounts by two BVI companies. The funds had ultimately stemmed from bribes paid to the former Mayor of Saõ Paulo and his son in connection with major infrastructure projects. The funds had been transferred through an account in New York, where they were mixed with other funds, before arriving in Jersey.

The difficulty was that not all of the monies which had flowed into the New York account could be traced directly into the Jersey accounts. The Court nonetheless held that the BVI companies were liable as constructive trustees for the whole sum transferred initially to the New York account, on the basis that where a court is satisfied that the various steps are part of a co-ordinated scheme, it should not matter (whether deliberately or because of the mechanics of the banking system) that the various debits and credits do not directly correspond with one another. We comment further on the significance of this decision in our eAlert on the case.

Appleby represented the trustees in the ABC Trust case and the plaintiffs in both the F Trust and Re a Settlement cases in Bermuda; the successful beneficiary applicant in the Piedmont trust case and the trustee of some of the trusts concerned in the Z Trusts case in Jersey; and in Cayman the trustee in the Schroder case and the appellant son in the Hinds case. Jersey partner Advocate Fraser Robertson also acted as Guardian ad litem for the minor and unborn beneficiaries in Representation of X Trustees Limited.

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