APPLEBY

PAPER

TRANSFER OF TRUSTEESHIP - DISCUSSION PAPER & CASE SUMMARY

By Ashley Fife

CONTENTS

PAPER

INTRODUCTION

Transfer of trusteeship often raises challenging issues for trustees. This paper explores the approach taken by courts in Bermuda and other jurisdictions in connection with the following issues and questions:

- The consequences and remedies when a trustee's appointment is invalid
- Is the power to appoint trustees always a fiduciary power?
- Improper exercise of the power to remove and appoint trustees
- The tension between the outgoing trustee's duty to transfer trust property and records verses its entitlement to security for its fees and liabilities
- When outgoing trustees may have personal liability for liabilities that exceed the value of the trust fund

The discussion paper uses a case study as a basis for exploration of the issues and to limit the scope of the paper. However, the intention is that, if need be, each part and section of the discussion paper may be referred to without having considered the case study in detail. Lists of cases with brief summaries, sections of legislation referred to and texts are provided at the end of the paper.

This is a rapidly developing area of the law and many cases turn on specific facts and differing judicial views. Accordingly, in each case, it is prudent to consider the specific facts and issues carefully and obtain advice as appropriate.

CASE STUDY: "POPEYE AND THE SINKING TRUST"

Spinach Unlimited, a BVI company controlled by Popeye, is the named settlor of the Sinking Trust, a discretionary trust established in 2004 governed by Bermuda law (**Trust**). Spinach Unlimited has the power to remove and appoint trustees.

Popeye's wife, Olive Oyl, and their children, are the Trust's beneficiaries. Dark & Stormy Trustees (Bermuda) Ltd (**D&S Trustees**) was appointed as trustee in 2008 when Harold Hamgravy, the original trustee, retired.

THE TRUST FUND

Assets:

- All the shares in Toot Toot Ltd, a BVI company.
- Unsecured loans of USD1.5 million owed by Spinach Unlimited (**Spinach Loans Receivable**).
- A portfolio of equity investments valued at about USD2 million (**Portfolio**), managed by Gonzalo Investments Ltd in Miami, the relationship manager being Popeye's good friend, Mr William J. Wimpey.

Liabilities:

- Toot Toot Ltd has made undocumented, unsecured loans of USD3 million plus interest to D&S Trustees over the years to help fund distributions, loans to Spinach Unlimited, and trustee fees and expenses (**Toot Toot Loans Payable**).
- D&S Trustees has USD40,000 in outstanding trustee fees. Popeye disputes the level of the fees.

Toot Toot Ltd

- In 2008, Popeye settled the entire share capital of Toot Toot Ltd into the Trust.
- In 2010, Toot Toot Ltd took out a large bank loan to buy a yacht, the Sea Hag. In 2012, the Sea Hag sank off St George's, in Bermuda. Toot Toot Ltd was unable to recover a significant portion of its losses from its insurers.
- In June 2014, Toot Toot Ltd was placed into insolvent liquidation. Mr Brutus is the appointed liquidator.

The SAR

In January 2014, D&S Trustees discovered Popeye had been indicted in the US for tax fraud and racketeering.

D&S Trustees' subsequently received repeated requests from Popeye to transfer funds into an account Spinach Unlimited has in South America. D&S Trustees considered it was unable to act upon Popeye's requests and was reluctant to communicate with Popeye for fear of tipping him off about the suspicious activity report it filed.

The Deed of Removal

In March 2014, D&S Trustees received a Deed of Removal executed by Spinach Unlimited to remove D&S Trustees and appoint as trustees Sweet Private Trust Company Ltd (**Sweet PTC**), a Bahamian private trust company.

Sweet PTC'S Demands

Later in March 2014, Sweet PTC wrote to D&S Trustees and insisted D&S Trustees urgently:

- transfer the Trust records and the Trust assets to Sweet PTC;
- provide explanations regarding a number of transactions; and
- provide copies of legal advice that D&S Trustees obtained in connection with a production order procured by the US Government under a TIEA.

D&S Trustees' Requests for Security

In late April 2014, in response to Sweet PTC's demands, D&S Trustees:

- told Sweet PTC to seek explanations of the Trust related transactions from Popeye;
- insisted that its fees be paid before it transfers any assets, records or provides any detailed explanations;
- requested Spinach Unlimited, the Trust's beneficiaries and Sweet PTC to release D&S Trustees from any claims they have against D&S Trustees in connection with the Trust; and
- stated it intended to retain the entire trust fund as security because it was concerned it may incur tax liabilities or costs in connection with further production orders.

Sweet PTC promptly responded and:

- asserted that D&S Trustees had produced no evidence of any potential tax liabilities;
- offered D&S Trustees an indemnity limited to the trust fund; and
- proposed that an amount be held in escrow pending determination of D&S Trustees' fees.

It's a long way to the ocean floor…

On 25 October 2014, D&S Trustees received:

- a letter from the former trustee, Harold Hamgravy, advising that Spinach Unlimited had been struck off the BVI Company Register at the time Spinach Unlimited executed the deed to appoint D&S Trustees in place of Harold Hamgravy; and
- a notice of claim from Mr Brutus claiming repayment of the Toot Toot Loans Payable.

PART 1 - INVALID APPOINTMENT OF TRUSTEES

Consequences of invalid appointments of trustees

If D&S Trustees' appointment was invalid, since 2008 it may have been dealing with the trust fund without the necessary authority (i.e. as a de facto trustee). This may bring into question its entitlement for all the fees it has charged and reimbursement for all the liabilities it has incurred, while purporting to act as trustee.

Harold Hamgravy may remain appointed as trustee and exposed for any losses caused to the trust fund by D&S Trustees' acts or omissions.

Section 23(a) of Bermuda's Limitation Act 1984 provides *inter alia* that no period of limitation shall apply to a beneficiary for actions against the trustee:

- for fraudulent breach of trust; or
- to recover trust property or its proceeds in the trustee's possession or converted to its use.

Aside from the above, section 23(3) of the Act provides *inter alia* the limitation period for breach of trust in Bermuda is 6 years from the date the right of action accrued.

Harold Hamgravy distributed the trust fund to D&S Trustees during 2008. It may be that the limitation period for a breach of trust claim against Harold Hamgravy has expired. However, Harold Hamgravy remains appointed as trustee and it may be argued that Harold Hamgravy's breach is viewed as an on-going breach and that the limitation period has not expired.

Purported exercise of powers by a struck off company's directors

Are there any quirks in BVI company law which may be relevant to the issue of the validity of D&S Trustees' purported appointment by Spinach Unlimited at a time when Spinach Unlimited was struck off the BVI company register?

Section 215 of the BVI Business Companies Act 2004 provides that when a BVI company is struck off, neither the company, nor any directors, may:

- act in any way with respect to the assets or affairs of the company; or
- claim any right for, or in the name of, the company.

However, if a BVI company has been struck off only for non-payment of annual government fees, the company may be restored to the company register within 10 years and, once restored, section 217 of the Act deems the company to have never been struck off the register.

Perhaps the consequence is that, upon Spinach Unlimited's restoration to the BVI Company Register, D&S Trustees' appointment will be treated as having always been valid.

However, if Spinach Unlimited was, for example, a Bermuda company, or a UK company, the position would be different. Reinstatement to the company register in those jurisdictions does not result in companies being treated as though they had always been on the relevant company register, in which case D&S Trustees' appointment would likely remain invalid.

What remedies are available for invalid appointments?

In a Jersey case of *In the matter of the D Retirement Benefit Trust* [2011] JLR 672, former directors of a UK company which had the power to appoint trustees, but had been dissolved, executed deeds to purportedly appoint trustees on the company's behalf:

- On one occasion, to replace a retiring trustee; and
- On another occasion, to appoint additional trustees.

Both appointments and the retirement were invalid. Consequently, the persons who had purportedly been appointed as trustees were considered to be acting as de facto trustees (or *trustees de son tort*) and the trustee who considered it had retired (by a deed of retirement and appointment) remained appointed as trustee. The de facto trustees and the outgoing trustee applied to the Court seeking remedies including:

- an order confirming the validity of the appointment of the (de facto) trustees or, alternatively, formally appointing the de facto trustees as trustees of the trust;

- ratification of the transactions implemented by the de facto trustees;
- rectification of the deed of retirement and appointment of trustees;
- relief of the outgoing trustees and the de facto trustees from liability in connection with the invalid deeds which had purported to effect the retirement and appointments as trustees; and
- approval of the outgoing trustee's fees.

The Court exercised its statutory powers and inherent jurisdiction to formally appoint the persons who had been acting as de facto trustees. In addition, the Court ratified the actions of the de facto trustees:

- because the Court determined the de facto trustees had acted in good faith and were unaware that they had not been properly appointed; and
- to save the trust from the havoc that might ensue from any attempt to unscramble what had been done by the de facto trustees.

The Court's ratification preserved the beneficiaries' rights to bring claims against the de facto trustees for breaches of trust other than those arising out of the invalid appointments.

The remedy of ratification made available *In the matter of D Retirement Benefit Trust* may represent another pragmatic "get of jail free card" for trustees. This pragmatism may be reminiscent of the remedy offered by the (pre UK Supreme Court *Pitt v Holt* and *Futter and Futter*) application of *Re Hastings Bass* and its statutory equivalents such as Bermuda's new Section 47A of the Trustee Act 1975 introduced during 2014. Francis Tregear QC, in his article *Putting it right: remedying problems arising from defective trustee appointment* (in Trust and Trustees, February 2013) makes the following comments regarding the decision *In the matter of D Retirement Benefit Trust*:

- The matter was not argued out adversarially as all parties sought ratification. Accordingly, care may need to be taken before placing great weight on the decision.
- The Jersey Court appeared to rely primarily on the Court's inherent jurisdiction as a basis for granting the remedy of ratification. However, UK courts (including the Privy Council) may not necessarily take as pragmatic or wide a view as offshore courts regarding the availability of the court's inherent jurisdiction as a basis for ratification.
- The wide jurisdiction offered by Section 47 of Bermuda's Trustee Act 1975 may enable the court to provide the trustees the power (once formally appointed) to ratify the transactions carried out by such trustees during the period that they had not been properly appointed.

Section 47 has become well known as a unique feature of Bermuda's trust law not offered in other jurisdictions. It has been used extensively for a variety of purposes to permit transactions not authorised by the trust deed (and to vary trust deeds) without consent of all of the beneficiaries in circumstances where a transaction is in the interests of the beneficiaries as a whole (or in the interests of one or more beneficiaries but of neutral impact on others).

In the matter of the D Retirement Benefit Trust, the Court also determined that the de facto trustees had acted honestly and reasonably and ought to fairly be relieved from liability. D&S Trustees and Harold Hamgravy may consider applying for such a remedy. The Bermuda Court has power to relieve trustees from liability under section 52 Trustee Act 1975 and as part of its inherent supervisory jurisdiction.

As an alternative to ratification, *In the matter of D Retirement Benefit Trust* the parties also sought rectification of the deed of retirement and appointment. The advantage of rectification was that it would have retrospective application so that the de facto trustees would be treated as though they had always been properly appointed and the retiring trustee's retirement effective. The arguments in favour of rectification were that:

- as the company had been dissolved, there was no one else who had the power under the trust deed to appoint trustees and therefore the outgoing trustee had the statutory power of appointment; and

- when it executed the deed, the outgoing trustee intended to divest itself of the office of trustee in favour of the incoming trustee.

Rectification is a discretionary remedy of the court exercising its equitable jurisdiction. In order to grant the order of rectification, the Court determined it needed to be satisfied that:

- as a result of a genuine mistake the deed of retirement and appointment did not reflect the true intention of the parties; and
- there was no other practical remedy.

The argument for rectification failed because the:

- outgoing trustee did not know it had the statutory power to appoint trustees at the time the deed was executed, therefore it could not have had the intention to itself appoint the new trustee; and
- Court was prepared to grant the remedy of ratification.

Do trustees have a duty to investigate capacity of their appointor?

Given the potential ramifications of an invalid appointment, should there be a duty on trustees to ensure that the person exercising the power to appoint trustees has capacity? Is it prudent for trustees to:

- obtain due diligence such as certificates of good standing?; or
- perform company searches on companies that are purporting to exercise a power to remove or appoint trustees?

In the matter of the D Retirement Benefit Trust, prior to its execution of the deeds, the directors of the (dissolved) company's holding company had mentioned to the outgoing trustee that the holding company was in the final stages of liquidation. However, the Court nevertheless determined that, as the outgoing trustee had acted honestly and in good faith, it was entitled to rely on the deed purportedly executed by the company under seal as a representation from the (dissolved) company's former directors that the company had capacity to enter the deed.

PART 2 - IS THE POWER TO APPOINT TRUSTEES ALWAYS A FIDUCIARY POWER?

Was Spinach Unlimited's appointment of Sweet PTC's a proper exercise of the power? At the time the appointment was made, Popeye had been seeking to effect transactions which:

- were not authorised by the trust deed; and
- may be construed as attempts to put assets beyond the reach of the US government.

Was Spinach Unlimited exercising its power for improper purposes when it purported to appoint Sweet PTC?

In *Bristol & West Building Society v Mothew* [1998] Ch1, Lord Millett LJ:

- defined a fiduciary as "someone who has undertaken to act on behalf of another in a particular matter in circumstances which give rise to a relationship of trust and confidence." [p16]; and
- expressed that "The distinguishing obligation of a fiduciary is the obligation of loyalty. The principal is entitled to the single-minded loyalty of his fiduciary." [p18]

If Spinach Unlimited's power to appoint trustees is fiduciary, it would have been under a duty to act in the interests of the beneficiaries of the trust at the exclusion of its own interests. If the power was personal, Spinach Unlimited may properly have taken into account its own interests subject to any express limitations in the trust deed regarding the scope of the power.

Re Skeats' Settlement

Since *Re Skeats' Settlement* (1889) 42 Ch the power to appoint trustees has generally been regarded as a fiduciary power. However, construction of the trust deed remains a primary consideration when categorising the power.

Skeats involved a marriage settlement and the Court:

- noted the trust deed did not express whether the power to appoint trustees was a fiduciary power or not;
- held the trust deed provided a requirement to appoint someone other than the power holder;
- considered, independently of the construction of the deed, that the power to appoint trustees was of its nature a fiduciary power and therefore those with the power could not appoint themselves; and
- determined that:

> "The ordinary power of appointing new trustees, under a settlement such as this…imposes upon the person who has the power of appointment the duty of selecting honest and good persons who can be trusted with the very difficult, onerous, and often delicate duties which trustees have to perform. He is bound to select to the best of his ability the best people he can find for the purpose."

Von Knierem v Bermuda Trust Co. and Grosvenor Trust Co.

In *Von Knierem v Bermuda Trust Co. and Grosvenor Trust Co*. [1995] S.C.B 154 (the "**Star Trusts' case**"):

- The power was held by the protector, Mr Von Knierem, the settlor's lawyer.
- The trust deeds did not express whether the power to appoint trustees was a fiduciary or personal power but did provide that the protector (who held the power) could not be a beneficiary and was excluded from receiving benefit from the trust.
- The protector exercised its power to replace Bermuda Trust Co. Ltd (**BTC**) with Grosvenor Trust Co. Ltd (**Grosvenor**)
- The settlor was a director of Corange Limited (**Corange**) in which the Star Trusts together held an interest;
- Corange's board made it clear they did not intend to re-appoint the settlor as a director at the upcoming annual general meeting.
- BTC was concerned that the protector would procure Grosvenor to vote at the AGM only taking into account the interests of the settlor rather than the beneficiaries as a whole.
- The protector and Grosvenor sought orders that BTC transfer the shares in Corange to Grosvenor and appoint the proxies to the AGM nominated by Grosvenor.
- BTC sought directions regarding the nature of the power and whether it had been properly exercised.

The Court considered the principles in *Skeats* and the construction of the trust deeds and held that the protector's powers were of a fiduciary nature largely because the protector was expressly precluded from receiving benefits from the trust.

Employers' powers and pension trusts

David Pollard, an experienced pensions lawyer and author of the book "The Law of Pension Trusts" has, in his book and a number of articles (including with Dawn Heath, "The power of employers to appoint or remove trustees of occupational pension schemes: is it fiduciary?" (2011) in Trust Law International) argues, in a pension trust context, that the power of appointment of trustees when held by an employer is not a fiduciary power other than in exceptional circumstances. The exceptional circumstances include where the:

- trust deed expressly provides that the power is fiduciary; or
- employer is also the trustee of the trust or holder of another fiduciary position.

The rationale supporting the argument that the power may not be a fiduciary power when in the hands of employers, broadly is that:

- the general position in relation to pension trusts is that employers' powers are not fiduciary (See generally, *Imperial Group Pension Trust Ltd v Imperial Tobacco Ltd* [1991] 2 All ER 597 and David Pollard's articles and text);
- the power to appoint trustees should not be categorised differently to other major powers such as a power of amendment;
- the powers of protectors, when also beneficiaries, are generally considered personal powers unless the trust deed says otherwise, albeit it has been suggested in *Re Circle Trust* [2006] CILR 323 and other cases that fiduciary elements nevertheless could apply to a protector's power to appoint or remove trustees;
- the approach in *Skeats*, which involved a marriage settlement, may not be appropriate for pension and other commercial trusts as they have materially different characteristics;
- an employer's position may be that of a quasi-beneficiary, as it has an interest in its employees receiving benefits from the pension scheme and is often entitled to receive a distribution of any surplus assets in the trust fund once members benefits have been fully satisfied;
- by analogy, the power to appoint and remove directors of companies is not regarded as a fiduciary power (see *Kuwait Asia Bank v National Mutual Life Nominees Limited* [1991] 1 AC 187); and
- even if the power is not fiduciary, employers are in any case subject to the duties:
    - to act in good faith and not to destroy the relationship of trust and confidence with its employees (often referred to as the "Imperial duty", from the abovementioned case of that name); and
    - not exercise the power for an improper purpose,

  therefore as a matter of policy it may be unnecessary to impose fiduciary duties on employers' exercise of powers to appoint trustees.

In the matter of the *HHH Employee Benefit Trust 2012* (2) JLR 64 the parties and the Court accepted, applying *Skeats*, that the power of appointment of trustees held by the settlor employer of an employee benefit trust was fiduciary despite the trust deed being silent as to the classification of the power.

There appears to be little authority where courts have determined that the power of employers to appoint and remove trustees was a personal power. Donovan Waters, in his article *Protectors and Enforcers*: *Drafting the Trust Instrument* [2000] JITCP pp237,252] acknowledges the possibility that the power to appoint or remove trustees may be personal in some circumstances.

It may be unusual for trust deed to provide that the power to appoint trustees is a personal power. However, on rare occasions, they specifically do or in other cases may include a blanket clause stating that all of the enforcer's or the protector's powers are personal powers. Some of these deeds may contain provisions which entitle the protector or enforcer to remuneration or exoneration, albeit such provisions may be inconsistent with a personal power. Would or should a court determine that the trust deed cannot categorise as a personal power what arguably is, by its nature, inherently a fiduciary power? Would or should a court permit an enforcer's or protector's receiver or bankruptcy trustee to exercise such personal powers in circumstances where they may do so for the purpose of ultimately amending the trust deed to facilitate distributions to be made from the trust to the enforcer or protector's creditors? These issues need to be considered if a decision is made to specifically categorise powers in trust deeds.

In the matter of the Bird Trusts

The classification of the powers to appoint trustees was considered in the Jersey case of *In the matter of the Bird Charitable Trust and the Bird Purpose Trust* [2008] JRC 013 (*Bird 2008*).

In *Bird 2008*, the Court considered that:

- whether a power is fiduciary or a beneficial personal power or a limited personal power is largely a matter for construction of the trust instrument to ascertain the nature and function of the power holder and the particular powers under scrutiny; and
- the power to appoint trustees is generally regarded as a fiduciary power even where the power is conferred on someone who is not a trustee, such as an unpaid protector who is connected to the settlor.

In *Bird 2008*, Mr Kaplan, the economic settlor of the trusts, was the trusts' protector and had the power to appoint trustees and his successor protector. The parties agreed that the power to appoint trustees was a fiduciary power.

In *Bird 2008,* the trust instrument provided that the protector:

- may be remunerated; and
- had the benefit of exoneration provisions.

These provisions indicated that the protector's powers were intended to be vested in an office holder rather than Mr Kaplan in his personal capacity.

Perhaps, we assume that the Sinking Trust trust deed does not:

- classify the power to appoint trustees as fiduciary or personal;
- include provisions for Spinach Unlimited (as power holder) to be exonerated from liability or to receive remuneration; or
- exclude Spinach Unlimited from receiving benefits from the Sinking Trust.

Spinach Unlimited is the settlor, is not a beneficiary of the Trust, but has been treated as a beneficiary as it has received a number of "soft" loans from the Trust. In the circumstances, it is submitted that Spinach Unlimited's power would nevertheless likely be categorised by a court as a fiduciary power unless there was a notable shift in the courts' approach. It is submitted that this conclusion would likely be reached in the circumstances (even if Spinach Unlimited was a beneficiary) in the absence of the trust deed specifying that the power is a personal power.

Bermuda and Section 2A(7) Trusts (Special Provisions) Act 1989

Bermuda's Trusts (Special Provisions) Amendment Act 2014 (**Amendment Act**), amended the Trusts (Special Provisions) Act 1989 to provide that certain powers, including the power to appoint and remove trustees, may be reserved to a settlor (or a protector or some other person) without invalidating the trust.

In addition, the Amendment Act inserted the new Section 2A(7) into the Trusts (Special Provisions) Act 1989 which provides that a Bermuda law trust created after the commencement of the Amendment Act, in the absence of contrary provision in the trust deed:

- in the case of reservation by a settlor, or the grant to a beneficiary of any of the powers specified, where so long as the power holder is not the sole trustee, such powers shall be personal and non-fiduciary; and
- in any other case, such powers shall be fiduciary.

The concern may be that, if the power to appoint trustees is a personal power, in the absence of express limits contained in the trust deed, the power holder may appoint itself or another person who may act in the power holder's interests as opposed to in the interests of the beneficiaries as a whole.

A trustee is a fiduciary and is under a duty to manage potential conflicts of interests (regardless of who appoints it) and to cease acting if an actual conflict of interests arises which would prevent it from fulfilling its duties. The situation may be analogous to that of a director who is appointed by a particular group of shareholders to represent their interests but fundamentally owes fiduciary duties to the company and not to those shareholders.

The Sinking Trust was established in 2004 (well before the Amendment Act became operative). Therefore Section 2A(7) does not apply to the Sinking Trust. It may be that outgoing trustees may owe very limited duties in relation

to power holders' exercise of personal powers to appoint trustees. For example, *Lewin on Trusts* (18th edition at 13-39) suggests, in relation to somewhat analogous circumstances, that, aside from exceptional circumstances, the outgoing trustee may have no duties to:

- investigate the suitability of the trustees that are appointed in its place by the power holder; and
- advise or warn beneficiaries, or decline to facilitate the appointment, even if it has concerns regarding whether the appointment is appropriate.

As reflected in *Lewin* (at 13-39) the exceptional circumstances may be if the:

- outgoing trustee receives actual notice of grounds for a serious objection regarding the suitability of the incoming trustee and the beneficiaries may be unaware of those grounds; or
- be vulnerable due to their age, mental capacity or some other reason. In those circumstances the outgoing trustees may be under duties to bring the grounds of objection to the attention of the beneficiaries or, where the beneficiaries are vulnerable, seek directions from the court.

It will be interesting to see what duties the courts consider may be owed by a person with the power to appoint trustees in circumstances where the power is deemed by Section 2A(7) to be a personal power. Perhaps, along the lines considered by Andrew Holden barrister in his book, *Trust Protectors* (Jordans, 2011, pp2.92 to 2.95) in circumstances where the trust instrument does not expressly state that the power to appoint trustees is a fiduciary power, the court may nevertheless construe provisions in the trust deed providing for the power holder's resignation, remuneration or exoneration as indicative of the settlor's intention that the power attaches to an 'office' (with fiduciary obligations) as opposed to a particular person to exercise for that person's own benefit.

PART 3 - IMPROPER EXERCISE OF THE POWER TO APPOINT TRUSTEES

In what circumstances will a court determine that a power holder's exercise of a power to appoint trustees is invalid? Does Spinach Unlimited intend to move assets beyond the reach of Bermuda regulation and the US government? Can it be inferred that Spinach Unlimited exercised its power to remove and appoint trustees for a purpose other than that for which the power was intended?

Von Knierem v Bermuda Trust Co. and Grosvenor Trust Co.

In the Star Trusts' case, the Court determined:

- an appointment of a trustee may be fraudulent and void if made for a corrupt purpose, such as to benefit the power holder;
- the onus is on the person seeking to avoid the appointment to prove an improper purpose;
- a mere possibility of benefit or improper motive (such as anger or resentment) will not suffice to demonstrate improper motive;
- Grosvenor was a reputable trust company and the trust property would not be at risk with Grosvenor as trustee; and
- there was no evidence that the power holder was exercising the powers for his own benefit or that the protector would control Grosvenor's exercise of its discretionary trustee powers.

In the matter of the Bird Trusts

In *Bird 2008*, the economic settlor and protector, Mr Kaplan had been indicted in the US for illegal gambling, racketeering and tax evasion. The trustee refused to implement transactions or communicate with Mr Kaplan for a period while it sought legal advice and regulatory consents. Mr Kaplan appointed successor protectors with the intent that new trustees, outside Jersey, would be appointed. The Court held that the exercise of powers to appoint

new protectors and new trustees did not amount to a fraud on the power notwithstanding that an objective of the appointment was to avoid Jersey regulatory issues which were delaying trust transactions.

The Court noted it was not a legal requirement for the trustees to obtain regulatory consents for the transactions but that doing so provided the trustees a defence if it was later determined that the funds distributed were proceeds of crime. The Court considered the decision would likely have been different had Mr Kaplan been convicted as the Court would not recognise an appointment made with the intention of committing a crime.

Sections 44(3)(b)(i) and 45(5)(b)(i) of Bermuda's Proceeds of Crime Act 1997 reflect a similar approach to that of Jersey's proceeds of crime legislation in this regard. Accordingly, there is an argument that in analogous circumstances, in the absence of conviction, a Bermuda Court may take a similar approach as the Jersey Court took in *Bird 2008*. However, in the case study, it may be open for a court to reach a different conclusion in circumstances where:

- Spinach Unlimited also appears to be seeking to procure transactions which are not authorised by the trust deed;
- Sweet PTC may be unlicensed and may be controlled by Popeye; and
- a court may have less confidence that Sweet PTC will exercise its powers independently than if a licensed trust company were appointed.

PART 4 - THE TENSION BETWEEN OUTGOING TRUSTEES' DUTIES AND ENTITLEMENTS

What are the outgoing trustee's duties?

Assuming the issues concerning the validity of Sweet PTC's appointment are overcome, we would need to then consider D&S Trustees' duties upon removal along with its entitlement to security.

At present, D&S Trustees does not appear to be facilitating the transfer of trusteeship at all. The issues surrounding the SAR and the validity of the appointments would be a basis for a delay until now. However, to what extent can a trustee who has been removed, with outstanding fees and concerns regarding its liabilities, refuse to transfer trust records and trust funds to the incoming trustee?

In the matter of Caversham Trustees and Andrew Crichton and in the matter of the Essel and Bruce Trusts [2008] JLR N [18] the Jersey Court considered that, from the date Caversham agreed to resign, it owed the following duties:

- quoting from *Ogier Trustees Limited v C.I Law Trustees Limited* [2006] JRC 158:

  > "In the transfer of trusteeship the outgoing trustee is under a duty to cooperate fully and actively in the transfer by making all relevant documents and correspondence promptly available to the incoming trustee and providing an explanation to questions reasonably raised by the incoming trustee." [p7]

- mobilise by taking necessary actions on a number of fronts with respect to the transfer process rather than working through issues consecutively;
- instruct lawyers to draft the deeds to transfer trusteeship and the assets;
- prepare the assets in readiness for transfer;
- ascertain the identities of entities to whom the assets are to be transferred;
- perform due diligence on the new trustee;

- where required obtain advice (in the jurisdictions in which the assets are situated) on the steps to effect the transfer and any tax and costs implications;
- setting out a timetable for the transfer of assets; and
- providing information to the incoming trustee to enable it to accept the assets.

The Court was critical of Caversham's approach of dealing with issues consecutively rather than pursuing actively a number of aspects to progress the transfer. In particular, the Court was critical of Caversham maintaining:

- it could not have begun the process of transferring assets until its indemnities were agreed; and
- that its fees must be paid before the transfer of assets took place.

The transfer of the trust property in Caversham took longer than 3 years from the date Caversham agreed to resign. The Court held this delay was excessive in the circumstances and determined:

- "When dealing with voluntary transfers between parties, albeit in the context of trusts, there is no way of arriving at an objectively correct date by which any particular asset should have been transferred;" [p39]
- a court will take into account the evidence and its view of the conduct of the parties when determining a reasonable time within which the assets should be transferred;
- that the transfer of assets should have been completed within 9 months Caversham's agreement to resign; and
- in circumstances where the delay was affecting the administration of the trusts, it was incumbent on an outgoing trustee to take initiative to apply to court to resolve the issues.

Escrow agents and outgoing trustees' outstanding fees

In the matter of the Carafe Trust [2005] JLR 159, the outgoing trustee, Guardian, and the settlor were in a fee dispute during the transfer of trusteeship. The incoming trustee, Herald, and the settlor proposed that an amount for the outgoing trustee's fees be transferred into an interest bearing escrow account and that the transfer promptly proceed.

However, Guardian responded saying it had provided a full breakdown of its fees and that transfer of trusteeship would not proceed until its fees were paid. Guardian also asserted that it had withdrawn its services. The Court observed that Guardian was ill advised to claim that it had withdrawn its services when no other trustee had been appointed in its place. Further the Court considered that it was unreasonable for Guardian to point blank reject the escrow proposal. The Court expressed:

> "Where a trustee is retiring but there is a dispute about fees, the trustee is entitled to arrangements which will ensure that it receives any fees ultimately to be found due but it is not entitled to greater protection than necessary. An escrow arrangement of the type proposed in this case will usually give a retiring trustee the required level of security." [p37]

Who may be indemnified upon a trustee's retirement or removal?

In the matter of Caversham the outgoing trustee accepted that it was appropriate to retire and that the assets be transferred to a new trust.

The Court noted that Article 34 if the Trusts (Jersey) Law 1984 provided that the duty to transfer assets is subject to the right of the outgoing trustee to be provided with reasonable security for its liabilities whether "existing, future, contingent or otherwise". Bermuda law does not have a similar statutory provision. However, the position in Bermuda may ultimately be similar, given (as recognised at 18-59 in *Lewin*) the trustees' general law entitlement to indemnification includes a lien (possessory and non-possessory) which:

- represents a proprietary interest in the trust fund;
- ranks above the interests of beneficiaries; and

- survives the trustee's resignation or removal.

Caversham prepared a deed of retirement, appointment and indemnity which included an indemnity to cover the outgoing trustee, the original trustee and their respective officers and employees. The Court took judicial notice that this part of the indemnity was accepted industry practice.

However, Caversham further extended the draft indemnity to:

> "any associates of both the retiring and the original trustee and of any and all companies incorporated in any part of the world whose shares form part of the Trust Fund."

The Court did not consider there was a legal basis for this extension, nor was it industry practice. The Court was critical of Caversham for its refusal to concede this point until more than 8 months had elapsed from the commencement of negotiations regarding the indemnity.

Therefore, it is suggested D&S Trustees, and outgoing trustees generally, should:

- carefully consider the reasons for rejecting an escrow arrangement for outstanding trustee fees;
- engage constructively in the transfer process, preparing for the transfer notwithstanding there are certain issues which require resolution;
- obtain advice regarding entitlement to indemnification and security as soon as possible; and
- consider an application to court if the inability to resolve the issues is impacting on the competent administration of the trust.

How does statutory automatic vesting impact on an outgoing trustee's security?

Section 30(1)(b) of Bermuda's Trustee Act 1975 provides for the automatic vesting of certain trust property (including the right to recover a debt or other thing in action) in the incoming trustees when the appointment is by deed. Under section 30(4) of the Act there are certain types of property which are not subject to the automatic vesting provisions including shares, annuities or property only transferable in books kept by a company or in a manner prescribed by statute.

This gives rise to two questions in relation to the case study:

- Is any of the trust property of the Sinking Trust of a nature which would automatically vest in the incoming trustees?
- Are D&S Trustees entitled to retain possession of property as security in circumstances where legal title has vested in Sweet PTC by virtue of the statutory automatic vesting provisions?

In response to the first question, The Sinking Trust fund consists of the Portfolio, the shares in Toot Toot Ltd and the Spinach Loans Receivable. The Portfolio and the shares in Toot Toot Ltd may require transfer of legal title by completing mandate changes, stock transfer forms and possibly new declarations of trust. These assets may not automatically vest in Sweet PTC by the Deed of Removal. The Spinach Loan Receivable may vest in Sweet PTC automatically by the Deed of Removal.

As to the second question, *Lewin* (at 14-49) expresses that an outgoing trustee may be compelled to transfer to the incoming trustee assets which are subject to automatic vesting thereby giving up its right of retention of trust property to secure its liabilities. The right of retention is intended to protect and interest of the trustee that has priority over the interests of beneficiaries. The outgoing trustee continues to have the benefit of an equitable non-possessory lien for its liabilities. However, non-possessory liens can be difficult and expensive to enforce, particular if the assets are not situated in jurisdictions that recognise the non-possessory lien. It may seem incongruent that an outgoing trustee would be required to give up its security by transferring possession of trust assets to an incoming trustee due to a statutory automatic vesting provision, only to have to incur considerable expense seeking to enforce a less certain equitable non-possessory lien.

Jersey and Guernsey have attempted to deal with the tension between automatic vesting and security by including in their trust legislation provisions which provide that an outgoing trustee's obligation to transfer trust property to the incoming trustee is subject to its retention of reasonable security for the outgoing trustee's liabilities. However, it may be that that UK and Bermuda Courts would adopt a different approach to that suggested in *Lewin*. The Law Reform Committee here in Bermuda is considering legislative reform which may further clarify that an outgoing trustee's obligation to transfer the trust property to incoming or continuing trustees is subject to the outgoing trustee's right to retain reasonable security.

Can trustees insist upon a release prior to transferring trust assets?

An outgoing trustee generally cannot insist upon a release from the incoming trustees or beneficiaries as a condition to transferring trust assets. However, the trust deed may include provisions which:

- exonerate the outgoing trustee from certain types of liabilities; or
- provide that the outgoing trustee's removal shall only be effective upon receipt of reasonable security for its liabilities properly incurred in connection with the trust.

It may be practical for trustees to negotiate the inclusion of exoneration provisions in the trust deed where possible before accepting trusteeship. It may be unreasonable to require the beneficiaries, settlor or the incoming trustee to provide a release at the time of the transfer of trusteeship as they may not have sufficient knowledge of any relevant claims to enable them to do so. From a practical perspective, it may be difficult for trustees to negotiate such releases when the relationship is coming to an end. Section 52 of the Trustee Act 1975 provides the Court the discretion to relieve the trustee from personal liability if the trustee has acted honestly and reasonably. However it is suggested that it may be more practical for D&S Trustees to focus on obtaining reasonable security for its liabilities rather than insisting upon a further release. D&S Trustees may seek to rely on exoneration provisions in the trust deed and ask a court to exercise its discretion under section 52 if a claim arises.

Should outgoing trustees retain trust documents as security?

Should an outgoing trustee refuse to provide trust documents and information to the incoming trustee pending an agreement for security for its fees and liabilities? It will be difficult for an incoming trustee to properly administer the trust if it does not have the relevant trust deeds and up to date accounts and other information.

In the matter of the Bird Charitable Trust and the Bird Purpose Trust [2012] JRC 006 (*Bird 2012*), the Jersey Court considered that:

> "…an outgoing trustee will normally be under a duty to hand over to the incoming trustee all documents and information which relate to the administration of the trust so as to enable the incoming trustee to fulfil its duties." [p29]

In *Bird 2012*, the incoming trustee argued that trust records were trust property and, because certain legal advice had been paid for out of the trust fund, the outgoing trustee was under a duty to provide the legal advice to the incoming trustee and the Court had no discretion to order otherwise.

The Court determined that:

> "In our judgment, the expression "trust property" refers to the assets in the trust which are being held for the benefit of the beneficiaries and may be paid or applied for their benefit. It is not possible to distribute legal advice; it is simply something which is obtained by the trustee in order to help him in connection with the administration of the trust. This is so even if the legal advice is paid for out of the trust property." [p21]

Given that trust records are not trust property, it is submitted a court is unlikely to be sympathetic of the retention of integral trust records as security for a trustee's outstanding fees and liabilities. A different approach, to that analogous to a professional exercising a lien over documents for outstanding fees, may need to be considered where that professional or other person is a trustee. However, this does not lead to the conclusion that an

outgoing trustee is obliged to provide the incoming trustee records and information at the outgoing trustee's own expense. *Sovereign Trust International Limited v WJB Chilterns Trust Company* [2005] JRC 004 confirms the outgoing trustee is entitled to its reasonable fees and expenses to provide the information and records.

An incoming trustee is under a duty to take reasonable steps to access the trust documents required to enable it to properly administer the trust. It may be unreasonable if an incoming trustee does not facilitate arrangements to pay or secure from the trust fund the outgoing trustee's reasonable fees and expenses in connection with providing trust records and information. However, there also may be instances where the outgoing trustee, arguably through mismanagement of the trust fund, has left the trust fund in a state where there are no liquid or other assets available as security for its fees and expenses. The quantum of any valid breach of trust claims against the outgoing trustee would be set off against the amounts for which the outgoing trustee may be properly indemnified. In these circumstances, an outgoing trustee may need to consider its position carefully when forming a view what, if any, remedy a court may be inclined to grant it in the circumstances.

Are there any documents outgoing trustees can refuse to provide to incoming trustees?

In *Bird 2012*, the Court confirmed the general rule is that an outgoing trustee has to provide the incoming trustee all documents and information relating to the administration of the trust which would enable the incoming trustee to fulfil its duties.

However, in *Bird 2012*, the Court expressed:

> "the Court has a discretion to direct that documents or information not be supplied where satisfied, in its supervisory role, that this is the appropriate course. The onus lies on the outgoing trustee to show why the normal rule should not be followed." [p29]

In *Bird 2012*, the outgoing trustee refused to provide legal advice paid for out of the trust fund which it obtained in relation to issues determined by earlier court proceedings. The Court accepted the outgoing trustee's argument that the legal advice was now irrelevant as a judgment had determined the issues considered by the advice and the issues were unlikely to arise again. However, the Court held the advice should be disclosed to the incoming trustee to enable it to fulfil its duty to determine whether the amount of the legal costs incurred and charged to the trust fund for such advice was reasonable.

There does not appear to be any compelling reasons for D&S Trustees to refuse to provide integral trust records to Sweet PTC subject to reasonable security being made available for its fees and expenses to provide the records.

Trustees' indemnification for remote liabilities

An assessment of what constitutes reasonable security for an outgoing trustee's liabilities involves consideration of:

- the nature and quantum of the liabilities;
- whether the liabilities are known or unknown, and if unknown, the likelihood they will crystallise;
- when the liabilities are likely to fall due; and
- the value of the assets proposed to be retained as security.

It may be that D&S Trustees is concerned that the incoming trustee is a private trust company (**PTC**) as opposed to a licensed trust company. PTCs generally do not hold assets of material value in their personal capacity, may not be insured, and may not have the resources to satisfy an indemnity if, for example, they breach the terms of the indemnity by distributing the trust fund without procuring indemnities in favour of the former trustee.

Sweet PTC's arguments may be that there is no evidence of any specific tax liabilities, that such liabilities are likely to materialise or, if any, the amount of such potential liabilities are unknown. However, simply because an amount of a liability is unknown, does not mean that the outgoing trustee is not entitled to security. Consistent with *Caversham*, the outgoing trustee is under a duty to seek advice where appropriate regarding tax liabilities in connection with the transfer of trusteeship. However, D&S Trustees are now concerned with more than just

remote tax liabilities. An indemnity alone, without retention of trust assets, would appear to be insufficient security for D&S Trustees' liability for the Toot Toot Loans Payable.

Oakhurst v Blackstar

In the UK High Court case of *Oakhurst v Blackstar* [2012] EWHC 1131 the outgoing trustee, Blackstar, believed that it may incur tax liabilities as a result of acting as trustee of an employee benefit trust which was established primarily to provide tax efficient benefits to directors of the settlor company. The outgoing trustee was unable to point to any specific tax liability. However, the Court considered that a reasonable professional tax adviser could not assess Blackstar's potential tax liability as nil. Justice Morgan also expressed:

> "I do not think that this is a case where the outgoing trustee should be left to bear whatever degree of risk there might be of a potential liability where it runs the further risk of there being no worthwhile indemnity in relation to it." [p72]

The trust deed provided that the power of removal was only effective upon reasonable security being provided for indemnifying an outgoing trustee against its liabilities. Consequently, when the settlor employer, purported to exercise a power to remove Blackstar, there was a dispute regarding whether Blackstar had effectively been removed as the indemnity offered arguably did not represent reasonable security.

The indemnity offered to Blackstar was limited to the trust fund in the possession of the incoming trustee from time to time subject to a requirement that the incoming trustee procure indemnities in favour of Blackstar from beneficiaries who may receive distributions. However, the trust assets consisted primarily of loans receivable due to the trustee from beneficiaries of the trust, the directors and former directors of the employer sponsor. Blackstar was concerned that the incoming trustee could reduce the trust fund without making distributions essentially by renegotiating the loans receivable so a lesser amount became due. It appeared likely that the incoming trustee would do so given the tax planning associated with the scheme.

The Court determined that reasonable security for Blackstar in the circumstances was an indemnity from the director beneficiaries and the settlor company. It is unusual for a court to order that a settlor and beneficiaries indemnify an outgoing trustee. However, the Court observed the settlor company and the directors stood to benefit from the structure and accordingly they should bear the risk of any potential tax liabilities.

Justice Morgan acknowledged how courts may vary in their assessment of the level of security which is reasonable for remote liabilities:

> "On my assessment it was quite a close call whether I should say that an indemnity that is worth very little will do for a liability that is very remote. I felt I could not say there was no risk and therefore there had to be something to cover it, not something illusory." [p84]

Based on *Oakhurst*, it may be reasonable that D&S Trustees perform reasonable investigations so it can better understand the amount of its potential tax liabilities. It is submitted that obtaining such advice is in the interests of the efficient administration of the trust to enable the issue of the outgoing trustee's security to be efficiently resolved. If D&S Trustees propose that the advice be a cost to the trust fund, it may be appropriate to share the instructions, fee estimates, invoices and the advice with Sweet PTC.

The Concord Trust case

The UK High Court case of *Concord Trust v The Law Debenture Trust Corporation plc* [2004] EWHC 1216 provided that if the outgoing trustees' liability is known, it can keep back the maximum and if it is unknown, it can keep back enough to cover the worst case, calculated on reasonable but not fanciful assumptions.

The *Concord* case, involved a trustee for bondholders of bonds issued by a Polish company guaranteed by the issuer's related entity, Elektrim. Subject to being indemnified to its satisfaction, the trustee was permitted to declare the bonds were due and payable in the event of the issuer's default on the notes. In earlier proceedings, of

which the issuer and the guarantor were not parties, a court determined that a default had occurred. The issuer informed the trustee that it disagreed with certain assumptions that Court had made regarding Polish law that the issuer considered relevant to the decision.

The trustee gave notice it would proceed with the declaration that the bonds were due and payable subject to being indemnified to its satisfaction. However, the trustee was concerned Elektrim may claim against it for wrongly making the declaration. Elektrim informed the trustee that, firstly, such a declaration would trigger a claim against Elektrim to sell its shares in another company at a significant loss and, secondly, it would seek to recover such losses from the trustee.

Concord, as representative of the bondholders, offered the trustee an indemnity guaranteed by a third party, Elliott. The trustee rejected the indemnity and requested an indemnity from the bondholders guaranteed by a letter of credit for EUR 1 billion from a major clearing bank for a period of 12 years.

The trustee had some concerns regarding the level and composition of Elliott's assets, how capital may be withdrawn from Elliott and how Elliots's assets may not be readily liquidated on demand.

Concord brought proceedings to compel the trustee to proceed with the distribution, arguing that no reasonable trustee would have rejected the indemnity offered. This test for reasonableness was developed from the case of *Associated Provincial Picture Houses Ltd v Wednesbury Corporation* [1994] 1 KB 223.

Concord argued that:

- There was no evidence to support that the trustee may be sued by Elektrim or anyone else for EUR 1 billion or that Elektrim could formulate such a claim.
- It was fanciful to believe that another court would reach a different decision to the Court which had determined that an event of default had occurred.
- There was no evidence to support that the trustee would not be able to successfully rely on the exoneration provisions in the trust deed.
- The right to indemnity in the trust deed did not entitle the trustee to require security.

The Court accepted the trustee's arguments that:

- The trustee's right to indemnification entitled it to security in the circumstances.
- Elektrim had an arguable claim against the trustee for breach of contract and that claim could amount to an award in the region of EUR1 billion.
- Elektrim may adduce evidence of the law in Poland which may impact on the determination of whether an event of default had occurred and it was not fanciful that a court may be persuaded by such evidence.
- The exoneration provisions in the trust deed did not exonerate the trustee for a breach of contract due its wrongful determination that an event of default had occurred.
- The indemnity in the trust deed from Elektrim and the issuer to the trustee did not cover claims from Elektrim.

In terms of the test for unreasonableness, in determining whether no reasonable trustee could have rejected Concord's offer, the Court considered the approach courts had taken in the analogous circumstances of a party's exercise of a discretion available to it under a contract. The Court quoted *Ludgate Insurance Company Ltd v Citibank NA* [1998] L1. L.R 221 and the statement that:

> "…provided that the discretion is exercised honestly and in good faith for the purposes for which it was conferred, and provided a trustee's exercise of the discretion… was not capricious or arbitrary or so outrageous in its defiance of reason that it can properly be categorised as perverse, the courts will not intervene." [p32]

Concord appealed the decision. In *Concord Trust –v- The Law Debenture Trust Corporation Plc* [2005] UKHL 27, the House of Lords:

- adopted the legal principles set out in the High Court's decision;
- on application of those principles to the facts, determined it was fanciful that the trustee may be considered negligent for declaring the bonds due and payable in circumstances where a court had determined that an event of default had occurred; and
- determined the indemnity and security offered by Concord and Elliot was such that no reasonable trustee would refuse it.

Concord is an example of the different views judges can have towards the adequacy of trustees' security for remote liabilities.

Can the outgoing trustee ever retain the whole trust fund as security?

As seen in the cases considered above and also *Re Knox's Trust* [1895] 2 Ch 483 (CA), the outgoing trustee is not automatically entitled to retain the whole trust fund as security. Doing so is rarely appropriate.

However, in the UK case of *X v A* [2000]1 All ER 490, the Court determined that, as the amount of the liability was wholly unknown, the trustee could retain the entire trust fund to secure its liabilities. In that case the trust fund consisted of land which may have been contaminated and under proposed new legislation, the trustee could potentially be liable for the clean-up costs.

The trustee sought directions regarding *inter alia* whether it:

- had a lien over the trust fund for its liabilities, including future and contingent liabilities; and
- may retain possession of the land.

The Court granted the orders and noted that the trustee's entitlement to a lien for its liabilities properly incurred had priority over the interests of the beneficiaries.

D&S Trustees may be concerned it has no meaningful security. The trust fund may include the Portfolio but it may be Gonzalo Investments recognise Popeye as its client, rather than D&S Trustees, despite the terms of the mandate. The other trust assets appear to be illiquid and potentially of little or no value.

D&S Trustees' liability to Mr Brutus under the Toot Toot Loans Payable are likely to exceed the value of the trust fund. This may be a case where the outgoing trustee may retain the whole trust fund.

PART 5 – TRUSTEES' PERSONAL LIABILITY & THE *GLENALLA* LITIGATION

It may be a paradox that the liquidator of Toot Toot Ltd is pursuing D&S Trustees for the Toot Toot Loans Payable in circumstances where D&S Trustees owns the entire share capital of Toot Toot Ltd.

Under Bermuda law, as is the case under English law, a trustee's liability is not automatically limited to the trust fund. Accordingly, trustees that enter contractual arrangements are wise to include suitable limited recourse clauses.

Jersey's and Guernsey's trust legislation each include provisions which broadly provide if a trustee makes known it is acting in its capacity as trustee to another party to a transaction then its liability to that other party will be limited to the trust property and the trustee will not incur a personal liability. While the relevant Guernsey and Jersey legislative provisions are not identical, there are material similarities between them for the purposes of the issues being explored here. Article 32 of the Trusts (Jersey) Law 1984 provides that:

"Trustees' Liability to Third Parties

(1) Where a trustee is a party to any transaction or matter affecting the trust-

(a) If the other party knows that the trustee is acting as trustee, any claim by the other party shall be against the trustee as trustee and shall extend only to the trust property;

(b) If the other party does not know that the trustee is acting as trustee, any claim by the other party may be made against the trustee personally (though, without prejudice to his personal liability, the trustee shall have a right of recourse to the trust property by way of indemnity).

(2) Paragraph (1) shall not affect any liability the trustee may have for breach of trust."

Bermuda's Law Reform Committee is considering whether Bermuda should introduce legislation with a similar objective to that of Article 32. However, even if such provision existed in Bermuda at the time D&S Trustees received the loans from Toot Toot Ltd, would such a provision provide absolute protection? If the loan constituted a breach of trust, then D&S Trustees not ordinarily be entitled to be indemnified from the trust property. However, there may be other limits to the protection such legislative provisions may provide.

This issue was explored in Guernsey case of *Investec Trust (Guernsey) Limited v Glenalla Properties Limited* unreported 6 December 2013, subsequently at the Guernsey Court of Appeal and, more recently, by the Privy Council. The Privy Council's judgment is greatly anticipated. The Tchenguiz Discretionary Trust (**TDT**) was funded by an appointment from another trust which was "related" to TDT by having the same settlor. Each trust was intended to benefit different sons of the settlor and their respective families.

The trustees of the related trust had, along with a number of its underlying BVI companies, agreed to a loan facility governed by English law. Under the loan facility each borrower guaranteed the other borrowers' obligations.

The related trust then appointed assets to the TDT including shares in the BVI companies. Investec and Bayeux as trustees of the TDT entered into separate deeds of novation whereby they assumed the liabilities of:

- monies owed by the related trust to some of the BVI companies; and
- the trustee of the related trust to a bank.

A number of the BVI companies went into liquidation. The bankruptcy trustees' demanded repayment of the loans from Investec and Bayeaux. Investec and Bayeaux were replaced as trustees of the TDT by Rawlinson Hunter. Investec and Bayeaux, were based in Guernsey and notwithstanding that the trust was governed by Jersey law, applied to the Guernsey Court seeking relief.

The trial Court determined that deeds of novation were not governed by the law of Jersey and that Investec and Bayeaux:

- had not acted in breach of trust and that they should be indemnified out of the trust property for the loan obligations;
- were unable to rely on Article 32 of the Trusts (Jersey) Law 1984 to limit their liability, in respect of the loans, to the trust property;
- were unable to rely on comparable provisions to Article 32, contained in section 42 of the Trusts (Guernsey) Law 2007, because section 42 did not apply to foreign law trusts; and
- were personally liable to the extent the trust property was insufficient to discharge the loans.

The Guernsey trial Court considered Guernsey's conflict of law provisions and determined it was not required to apply Jersey law to determine Investec and Bayeaux's obligations under the loans because the issue did not relate to enforcement of the trusts but enforcement of a transaction concerning the trusts.

However, it was held by the Guernsey Court of Appeal in *Investec Trust (Guernsey) Limited v Glenalla Properties Limited* 28/2014:

- The Guernsey Court's ability to apply the law of a foreign law trust was not limited to matters of enforcement of the trust.
- Where the law of one jurisdiction makes provision regarding the potential liability of persons holding a particular status, those provisions, if of a substantive nature (such as Article 32) will be recognised by the courts of the forum of dispute.
- A party to a transaction who is aware that it is contracting with another party of a particular status needs to consider the laws of that entity's jurisdiction notwithstanding the governing law of the transaction.
- It would be perverse not to apply Jersey law for the trustee's benefit in circumstances where the Trusts (Guernsey) Law 2007 includes section 42 which is similar to Article 32 of the Jersey statute.
- Given their relationship it was implicit that the parties to the transaction intended to limit the personal liability of the trustees to the trust fund.

Professor David Hayton, in *A 2014 Review of Recent Trust Law Developments*, in Trust Law International, has criticised the Guernsey Court of Appeal's approach of likening a trust to a company acting through agents and treating the issue of the trustee's liability under the contracts as one of trust law rather than contract law. He considers that UK courts may not approach the matter the same way. The Privy Council's judgment is awaited. The impact of this type of legislation is far from settled. Even so, given the relationship between D&S Trustees and Toot Toot Ltd, there may be a persuasive argument it was an implied term that D&S Trustees liability would be limited to the trust fund. This argument could be made despite the absence of a statutory equivalent to Jersey's Article 32 or Guernsey's section 42 in Bermuda. However, it is far from ideal to have to rely on a court's willingness to imply such a term.

CONCLUSION

The discussion explores a number of cases in some detail. The assessment of a how a court may resolve the issues in the case study may be relatively brief. The journey is more important than the destination for these purposes. While we do not have all the facts and inevitably a number of assumptions may need to be made, it is submitted that:

- If D&S Trustees' appointment was invalid, its actions as de facto trustee may be ratified insofar that they would not have otherwise constituted breaches of trust.
- D&S Trustees may be entitled to its reasonable administration fees.
- Harold Hamgravy may be released from any liability arising from his potentially invalid retirement.
- Sweet PTC's appointment may well be invalid.
- However, assuming Sweet PTC's appointment was valid, D&S Trustees would be entitled to reasonable security for its fees and the Toot Toot Loans Payable but would be compelled to transfer the trust records to Sweet PTC.
- D&S Trustees' liability for the Toot Toot Loans Payable would be limited to the trust fund (subject to the Privy Council's decision in *Glenalla*).

Perhaps the most certain aspect of any proceedings to determine all the issues raised by this case study is that, whatever the decision, there will be scope for an appeal.

The importance of ensuring that deeds of appointment, retirement or removal of trustees are properly executed and otherwise valid cannot be underestimated. The legal fees in connection with remedial work (which may include court proceedings) along with the uncertainty of achieving the desired remedies, will almost always dwarf the costs involved in getting it right in the first instance.

The importance of trustees checking the value and nature of the trust fund and the extent of their control over trust assets before entering transactions, even related party transactions, cannot be understated. There may be statutes that offer trustees some assistance when things go wrong but prevention, including that in the form of suitable limited recourse language in transaction documents, may provide better protection than a statutory provision which may or may not provide a cure.

The classification of powers as fiduciary or personal is often not straightforward and reserved powers legislation has been a catalyst for further analysis of this subject by the courts. The consequences of trust deeds labelling powers as fiduciary or personal needs to be considered carefully, especially given that receivers and bankruptcy trustees may have more than reasonable prospects of utilising such insolvent person's powers to access trust property.

Reasonableness (including proportionality) and the interests of beneficiaries and the efficient administration of the trust are all at the heart of determining issues relating to the transfer of trusteeship, not least the issue of the adequacy of an outgoing trustee's security for its liabilities properly incurred. The inherent problem may be that perspective cannot be divorced from even a court's assessment of what is objectively reasonable.

The introduction of unique reserved powers and "Hastings Bass" legislation has been a coup for Bermuda's trust industry in 2014. There are other projects afoot to reinvigorate and maximise the potential of Bermuda's already strong platform as a trust jurisdiction. A number of such proposed reforms are being considered which would impact upon the transfer of trusteeship. 2015 will be a year of "watch this space" as far as Bermuda and this subject are concerned.

PART 6- CASE LIST AND REFERENCE MATERIAL

CASE LIST

1 ***Re Knox's Trust*** **[1895] 2 Ch 483 (CA)-**

Outgoing trustees are not automatically entitled to retain the entire trust fund as security for their liabilities.

2 ***Re Skeats' Settlement*** **(1889) 42 Ch D-**

Considered the inherently fiduciary nature of the power to appoint trustees in the context of a marriage settlement.

3 ***Associated Provincial Picture Houses Ltd v Wednesbury Corporation*** **[1948] 1 KB 223-**

The Court developed test for reasonable exercise of discretion of a local authority. An exercise of discretion would be reasonable if it was not an exercise of which no local council could consider reasonable.

4 ***Tiger v Barclays Bank*** **[1952] 1 All ER 85-**

"If such a document relates to the administration…and no more than that is known about it, then, at all events, it is potentially a document which would or might assist the [*incoming trustee*] in the administration of the estate [*or the trust*]. Whether it would in fact do so or not must depend on its actual contents and, on that question, *prima facie*, the plaintiffs, whose duty it is to carry on the administration, would be the best judges, and obviously they could only form an opinion by looking at the document itself." [p88][*Our addition*].

5 ***Imperial Group Pension Trust Ltd v Imperial Tobacco Ltd*** **[1991] 2 All ER 597-**

The Court considered that employers owe a duty of good faith not to destroy the relationship of trust and confidence with its employees when exercising powers under a pension trust deed.

6 ***Kuwait Asia Bank v National Mutual Life Nominees Limited*** **[1991] 1 AC 187-**

The Court considered the power to appoint directors was not a fiduciary power.

7 ***Von Knierem v Bermuda Trust Co. and Grosvenor Trust*** **[1995] S.C.B (also known as the "Star Trusts' case")-**

The Court considered the:

- fiduciary nature of power to appoint trustees on construction of trust deed; and
- proper exercise of power to appoint trustees.

8 ***Bristol & West Building Society v Mothew*** **[1998] Ch1-**

Lord Millett LJ:

- defined a fiduciary as "someone who has undertaken to act on behalf of another in a particular matter in circumstances which give rise to a relationship of trust and confidence." [p16]; and
- expressed that "The distinguishing obligation of a fiduciary is the obligation of loyalty. The principal is entitled to the single-minded loyalty of his fiduciary." [p18]

9 ***X-v-A*****, B, C [2000] 1 All ER 2000-**

The Court determined that the outgoing trustee could retain the entire trust fund as security in the exceptional circumstances.

10 ***In the Matter of the Carafe Trust-Guardian Trust Company -v- Louveaux & Four Others*** **[2005] JLR 159-**

The Court considered that escrow arrangements are generally suitable as security for outgoing trustees' outstanding fees.

11 ***Concord Trust –v- The Law Debenture Trust Corporation Plc*** **[2004] EWHC 1216 (Ch)-**

Outgoing trustees can retain the full amount required to cover their known liabilities. If the amount of a liability is unknown, outgoing trustees can keep back enough to cover the worst case scenario, calculated on reasonable but not fanciful assumptions.

12 ***Concord Trust –v- Law Debenture Trust Corporation PLC*** **[2005] UKHL 27-**

As above, but the House of Lords took view that the security offered to the outgoing trustee was such that no reasonable trustee should refuse it.

13 ***Southern Wine Corp. Pty Ltd –v- Frankland River Olive Co. Ltd*** **[2005] WASCA 236-**

The Court determined a trustee's entitlement to indemnity survives its loss of trusteeship.

14 ***Sovereign Trust International Limited –v-WJB Chilterns Trust Company*** **[2005] JRC 004-**

The Court recognised the Trustee's entitlement to reasonable fees and expenses for providing trust documents and information.

15 ***Ogier Trustees (Jersey) Limited –v- C.I Law Trustees Limited & C.I Law Trust Group Limited*** **[2006] JRC 158-**

The Court determined that outgoing trustees are under a duty to cooperate actively in the transfer by making documents and information available to the incoming trustees.

16 ***J. Landau –v Auburn Trustees Limited, A. Landau, C. Landau & R. Landau*** **[2007] JRC 250-**

In this case the invalidly appointed (de facto) trustees were awarded their administration fees and legal costs as they had provided trustee services honestly in good faith.

17 ***In the matter of The Bird Charitable Trust and the Bird Purpose Trust*** **[2008] JRC 13-**
Basel Trust Corporation (Channel Islands) Limited –v- Ghilandina Anstalt & Larona Trust Reg, Roenne Corporation & Gary Kaplan **2008 JLR 1-**

The Court determined the nature of the power to appoint trustees and successor protectors, on construction of trust deed, were fiduciary powers. The Court considered the proper exercise of the power to appoint successor protectors and trustees in the context of settlor's indictment for illegal gambling and tax fraud.

18 ***In the matter of the E, L , O & R Trusts-***
BA, SA & HA –v- Verite Trust Company Limited, Appleby Trust Company Limited & James **[2008] JRC 360-**

The Court awarded costs against the trustee seeking directions regarding whether it should retire in circumstances where the trustee plainly had a conflict of interest and should have retired.

19 ***GH and IJ v KL and Others*** **[2010] Bda LR 86-**

Section 47 of Bermuda's Trustee Act 1975 permits the Court to authorise transactions in circumstances where the transaction is in the interests of one beneficiary but of neutral impact on other beneficiaries.

20 ***In the matter of the Representation of BB, A & C-In the matter of the D Retirement Benefit Trust*** **[2011] JRC 672-**

The Court considered ratification, rectification, costs and other orders where (de facto) trustees' appointments were invalid. The Court relieved the de facto trustees' from liability, ratified their actions and were awarded their reasonable legal and administration costs.

21 ***In the matter of the Bird Charitable Trust & the Bird Purpose Trust-***
Equity Trust (Bahamas) Limited –v- Basel Trust Corporation (Channel Islands) Limited **[2012] JRC 006-**

The Court recognised that trust records are not trust property and considered circumstances when Court may exercise discretion to refuse to order an outgoing trustee to disclose legal advice and other trust records paid for by the trust fund. The Court ordered the legal advice be disclosed in order that the incoming trustees could, in satisfaction of its duties, determine whether the costs incurred in obtaining it were reasonable.

22 ***Oakhurst Property Developments & others –v- Blackstar (Isle of Man) Limited & Church Street Trustees Limited*** **[2012] EWHC 1131-**

The Court considered an outgoing trustee's security for remote liabilities. The Court acknowledged that different views may be reached but ordered settlor and beneficiaries to indemnify outgoing trustee.

23 ***In the matter of the HHH Employee Trust- In the matter of the B Sub-Trust-B v C & E*** **[2012 (2) JLR 64-**

The parties accepted the employer's power to appoint trustees was a fiduciary power.

24 ***Investec Trust (Guernsey) Limited & Bayeux Trustees Limited–v- Glenalla Properties Limited* & *Rawlinson & Hunter Trustees* S.A. Guernsey Royal Court. Unreported. 6 December 2013. 38/2013-**

At first instance, the Guernsey Court determined that the trustees of a Jersey law trust were not entitled to rely on Article 32 of the Trusts (Jersey) Law 1984 in a Guernsey Court to limit their liability to the trust fund for certain debt obligations (which were not governed by the law of Jersey).

25 ***Investec Trust (Guernsey) Limited & Bayeux Trustees Limited–v- Glenalla Properties Limited & Rawlinson & Hunter Trustees S.A.* Guernsey Court of Appeal 28/2014-**

The Guernsey Court of Appeal held that outgoing trustee's liability to underlying companies' was limited to the trust fund as such was implicit in the agreements and due to the application of Article 32 Trusts (Jersey) Law to limit the outgoing trustee's liability to the trust property.

STATUTORY PROVISIONS

Bermuda

Section 30 Trustee Act 1975-

Automatic vesting of certain types of trust property where trustee appointed by deed.

Section 31 Trustee Act 1975-

Court's may, if expedient, appoint new trustees where it is difficult to do so without Court's assistance.

Section 32 Trustee Act 1975-

Court's power to authorise remuneration for acting as trustee.

Section 52 Trustee Act 1975-

Court's power to relieve trustee from personal liability for breach of trust where trustee has acted honestly and reasonably and ought fairly be relieved from liability.

Section 2A(7) Trusts Special Provisions Act 1989, as amended by Trusts (Special Provisions) Amendment Act 2014-

Deems reserved powers to be personal, non-fiduciary powers, unless the trust deed expresses a contrary intention.

Sections 44(3)(b)(i) and 45(b)(i) of the Proceeds of Crime 2007-

Provides a person defences to money laundering and related offences where that person has obtained the consent of the Financial Intelligence Agency prior to making or facilitating a transaction.

Jersey

Article 32 Trusts (Jersey) Law 1984-

Limitation of trustees' liability to trust property to third parties if trustee makes known acting in capacity as trustee.

Article 34 Trusts (Jersey) Law 1984-

Trustees' duty to surrender trust property to incoming trustee upon receiving reasonable security for its liabilities.

Guernsey

Section 42 Trusts (Guernsey) Law 2007-

Limitation of trustees' liability to trust property to third parties if trustee makes known acting in capacity as trustee.

Section 43 Trusts (Guernsey) Law 2007-

Trustees' entitlement to retain reasonable security before surrendering trust property.

British Virgin Islands

Section 215 BVI Business Companies Act 2004-

Restricts a director, liquidator or receiver of a company's dealing with assets and commencing or defending claims for the company.

Section 216 BVI Business Companies Act 2004-

Where a company is struck of the BVI company register under section 213 of the Act and remains struck off for a continuous period of 10 years, it is dissolved with effect on the last day of the period.

Section 217 BVI Business Companies Act 2004-

A struck off company which has not been dissolved may, upon satisfaction of certain conditions, be reinstated to register and deemed to have never been struck off.

BOOKS, ARTICLES AND GOVERNMENT PAPERS

The Trust Law Committee of England and Wales, *The proper protection by liens, indemnities or otherwise of those who cease to be trustees*, Professor D Hayton (Chair), December 1999.

Underhill and Hayton, *Law relating to Trust and Trustees*, Butterworths, 17th edn, (2006)

Lewin on Trusts, Sweet & Maxwell, 17th edn (2000) and 18th edn (2008)

Pollard, D Heath, *The power of employers to appoint or remove trustees of occupational pension schemes: is it fiduciary?*" (2011) in Trust Law International.

Holden A, Brownbill D QC (Consultant Editor), *Trust Protectors*, Jordans, 2011.

A Practical Guide to the Transfer of Trusteeship (Ed. R Williams, A Saker, T Graham), Society of Trust and Estate Practitioners, 2011.

Ratcliffe H, *Trusteeship changes and asset valuation points*, Trust and Trustees, 13 October 2011.

Tregear F QC, *Putting it right: remedying problems arising from defective trustee appointment,* Trusts and Trustees, Vol. 19, No. 1, February 2012, pp23-30.

Booth M QC and Bourne R, *How secure is security*?, Trust and Trustees, vol. 19, No. 5, June 2013, pp475-480.

Hayton D, A 2014 *Review of Recent Trust Law Developments,* Trust Law International, 28(2), 51-64 (2014).

PAPER

This discussion paper has been written by:

Ashley Fife
+1 441 298 3221
afife@applebyglobal.com

21 December 2014

Lawyer Ashley Fife is a Senior Associate and a member of the Private Client and Trusts Practice Group at Appleby in Bermuda.

This discussion paper should not be used as a substitute for professional legal advice. Before proceeding with any matters discussed here, persons are advised to consult with a lawyer.