serle speak
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Welcome to the new edition of Serle Speak. This time the subject is trusts. The edition begins with my article on the characterisation of trusts as *inter vivos* or testamentary, particularly where the settlor retains control. Richard Walford also discusses the position of the settlor, this time in relation to a settlor's power to appoint protectors. Elsewhere Giles Richardson looks at the problems faced by trustees in respect of ancillary relief and bankruptcy proceedings, and Dakis Hagen considers an important development in the law of knowing receipt and limitation. Finally, Professor Jonathan Harris addresses the tensions between EU law and the engagement of English courts with offshore trusts. **FRANK HINKS QC**

Trusts ineffective as testamentary dispositions

A DOCUMENT WHICH IN OUTWARD FORM IS AN *INTER VIVOS* DISPOSITION MAY BE A "TESTAMENTARY DISPOSITION" AND HENCE SUBJECT TO THE WILLS ACTS.

In the anonymised Bermudan case of *Q v Q* [2010] the purported settlor was a businessman who wanted to settle company shares on two *inter vivos* trusts for his issue, but reserving to himself complete benefit and control during his lifetime. The trusts although expressly governed by Bermudan law were in US form with the settlor as donor purporting to contract with himself as sole trustee but in substance declaring himself trustee. By Article I he reserved power to revoke or amend the trusts in whole or in part by instrument signed by himself as donor and delivered to himself as trustee. By Article II he was entitled to the entire net income during his life and to so much of the capital as the trustee (i.e. himself) should in the trustee's absolute discretion determine. The trusts for his issue in Article III were expressly stated to come into effect upon his death: during his lifetime no one but himself could benefit. Most remarkably (and fatally for the purported trusts) Article VIII H provided that the written approval by the settlor of any trust transaction during his lifetime should be a complete release of the trustee (including the settlor) of any liability or responsibility of the trustee to any person with respect to the transaction: retrospectively or prospectively the settlor could bless any transaction carried out by himself as trustee even if effected fraudulently or in bad faith contrary to the interests of all beneficiaries other than himself and hence in flagrant breach of trust.

Ground CJ held that the trusts failed on two alternative bases.

First, it is well established that for a trust to exist there must be enforceable rights and obligations as between the beneficiaries and the trustees. As Millett LJ stated in *Armitage v Nurse* [1998] Ch 241 at 253:

"If the beneficiaries have no rights enforceable against the trustees there are no trusts."

The trusts declared in Articles I and II to take effect during the settlor's lifetime were void on the face of the documents for want of enforceability/accountability. As Ground CJ stated at paragraph 29:

"my primary conclusion is that the concatenation of rights and powers in the settlor, when coupled with the fact that he was the sole trustee at the time of the constitution of the Trusts, rendered this trust illusory during his lifetime. …… the cumulative effect of the trust documents, when taken with the *de facto* situation, means that the settlor as trustee could not effectively be called to account during this lifetime. Crucial to this conclusion is Art.VIII H, which allows the settlor to absolve himself as trustee from any and all breaches of trust."

The consequence of there being no trusts effective during the settlor's lifetime was that the remaining trusts (which were stated on the face of the trust instruments to take effect from the settlor's death) were testamentary in nature. Normally in this situation the trusts determined to be testamentary in nature fail for want of due execution in accordance with the Wills Act. In this case by an unusual chance the settlor signed the trust agreements twice, once as donor and once as trustee. Each signature was witnessed by a different person, each such person probably being present at the same time and hence, at least arguably execution complied with testamentary formalities. This was not enough to save the trusts: they were revoked by the settlor's second marriage which was subsequent to the execution of the trust agreements.

Secondly, in determining whether an instrument is a testamentary disposition the court is not limited to considering the form of the instrument but may consider external evidence including evidence as to the settlor's intention. Having regard to the evidence external to the trust agreements, Ground CJ concluded that it was not the intention of the settlor to fetter his unhindered control and enjoyment of the settled assets during his lifetime, that he did not have the necessary intent to create a trust during his lifetime and in consequence the trust instruments were testamentary dispositions revoked by his subsequent marriage.

The modern trend (in particular in offshore jurisdictions) is to maintain the validity of declared trusts, but as *Q v Q* demonstrates there is an irreducible core of obligations owed by the trustees to the beneficiaries and enforceable by them which is fundamental to the concept of a trust and an *inter vivos* trust can fail as an invalid or revoked testamentary disposition.

An interesting issue is whether the combination of the settlor as sole trustee, the settlor as sole beneficiary during his lifetime and the settlor retaining power of revocation would have been sufficient to render the trusts declared in Articles I and II void on their face without Article VIII H. The mere retention of power of revocation will not normally of itself render a trust a testamentary disposition even if the settlor is sole beneficiary during his lifetime provided the trustees are persons other than the settlor. If the settlor is sole trustee there are in reality no enforceable obligations prior to his death: he can prevent any claim by other beneficiaries against himself as trustee by revoking the trusts and does not owe any enforceable obligation towards himself as beneficiary. Nevertheless, in the light of the modern attitude of maintaining the validity of trusts *Q v Q* may be treated by future courts as limited to its special and rather unusual facts and given only limited application.

FRANK HINKS QC was Leading Counsel for the Plaintiffs in *Q v Q* successfully arguing for invalidity. He specialises in domestic and international trusts.

Calling a divorcing beneficiary's bluff

AN UNEXPECTED BUT NOT INFREQUENT ISSUE FACING TRUSTEES IN THE CONTEXT OF ANCILLARY RELIEF PROCEEDINGS WHERE ONLY ONE SPOUSE (USUALLY STILL THE HUSBAND) IS WITHIN THE TRUST'S BENEFICIAL CLASS IS A THREAT BY THAT SPOUSE TO DECLARE HIM OR HERSELF BANKRUPT.

This often appears to be an effort to thwart a proposed appointment of trust monies to the wife or release security held by the trust over property in the husband's name. Such threats, even if carried out, ought not of themselves to deflect the trustee from proceeding to make the appointment or to release the security (if approved by the Court).

The impact of bankruptcy on ancillary relief orders

In the first place, this is because the bankruptcy process is in fact irrelevant to the ancillary relief process. True it is that, once a bankruptcy process has been completed, a bankrupt will obtain his discharge from bankruptcy. The effect is to free him from "bankruptcy debts". But by section 281(5) of the Insolvency Act 1986 ("IA"), discharge does not of itself release the bankrupt from a bankruptcy debt arising under an order made in family proceedings. "Family proceedings" are then defined as including matrimonial causes.

So simply seeking his own bankruptcy will not assist the spouse determined to evade what he or she regards as "their" trust benefitting their former spouse.

The trustee and preferences

Whilst this is so, nonetheless beneficiary-spouses have sought to dissuade trustees from taking steps in relation to ancillary relief orders by more sophisticated arguments. In particular, he may argue that action by the trustee to release security or appoint funds in favour of a spouse would be a preference in her favour.

The relevant statutory provision in England is section 340 IA.

In brief summary of this section, there are a number of fundamental requirements of the jurisdiction which would have to be satisfied before a preference would be found to exist:

(1) the beneficiary himself will have had to have given the preference by doing something himself or "suffering anything to be done" which has the effect of preferring someone – here his (former) spouse;

(2) that person must be a creditor or surety or guarantor of his at the time the preference is given; and

(3) he must have been influenced by a desire to prefer his spouse.

What would happen, however, is that the trustee would appoint funds to the spouse having taken a decision in which the beneficiary would play no part and which he is powerless to stop, in circumstances where he has protested against any benefit being conferred at all. Given this, it seems extremely unlikely that any preference claim could succeed:

(1) the beneficiary would not thereby have "suffered" anything to be done;

(2) he had not been influenced by a desire to prefer his wife (notwithstanding the rebuttable presumption in subsection (5)); and

(3) if the ancillary relief order had not yet been made, the trustee in bankruptcy would face firm

authority – and sound principle – against the proposition that a spouse with a mere expectation of receiving ancillary relief was a creditor within the provision: see *Re Jones* [2008] BPIR 1051 and the commentary on section 340(4) and (5) in *Sealy & Milman's Annotated Guide to Insolvency Legislation*.

Given the above, threats by a beneficiary to cause his own bankruptcy can generally be regarded with equanimity by trustees faced with the manifold other complications which arise when ancillary relief proceedings involving a beneficiary are begun.

GILES RICHARDSON regularly acts for and advises trustees in relation to a wide range of trust issues.

What you don't know can't hurt you

THE ROYAL COURT OF JERSEY IN *BAGUS INVESTMENTS LIMITED V KASTENING* HAS RECENTLY HANDED DOWN A VALUABLE JUDGMENT ON KNOWING RECEIPT AND THE RELATED LAW OF LIMITATION

Bagus Investments and Dr Wilfried Kastening had both been clients of a company administrator which had gone under because of fraud. Bagus alleged that it could trace funds stolen from it to monies which had been in the hands of Dr Kastening.

Dr Kastening was sued under the no-fault restitutionary principle recognised in *Re Esteem*. But then, nearly 13 years after the event, the plaintiff sought to amend to claim knowing receipt. Bagus pleaded that Dr Kastening had feared that, first, the monies he had received could be frozen, and second that he could be pursued for repayment. Although he did not have actual knowledge of the particular transaction in breach of fiduciary duty, he had allegedly failed to make enquiries. Further it was contended that there was no limitation period.

Dr Kastening resisted the amendment successfully. The case engaged the much-debated distinction between class 1 constructive trustees (persons who take possession of trust property assuming obligations to others) and class 2 constructive trustees (persons who receive property only following an unlawful transaction impugned by the plaintiff). Dr Kastening said that the statutory provision preventing trustees from pleading limitation in fraud and conversion cases only applied to class 1 constructive trustees. Dr Kastening, if liable, was in class 2. Bagus said that the authorities were not settled on the point. Also, Bagus submitted, there was a Jersey provision whose effect was to deem a knowing recipient a trustee for limitation purposes.

Birt B held that while the authorities had "not invariably spoken with one

> "The court approached with rigour what the defendant must be alleged to have known"

voice… the overwhelming likelihood is that English law considers that class 2 constructive trustees… are not trustees for the purposes of … the Limitation Act". After comparing English to Jersey legislation he held that the similarities were such as to provide a "strong basis" for applying the class 1/class 2 reasoning to its interpretation.

Further the Bailiff held that the pleading did not meet the necessary standard; it inadequately set out Dr Kastening's knowledge of the original fraudulent payment. The court thus approached with rigour the test in *BCCI v Akindele*, focusing on what the defendant must be alleged to have known. Receipt of assets traceable to a breach of fiduciary duty plus generalised allegations of unconscionability will, it seems, not be enough for a sustainable claim.

DAKIS HAGEN advised Dr Kastening, the successful respondent.

Protector appointments: Does the settlor owe fiduciary duties?

MANY TRUST DEEDS EMPOWER THE SETTLOR TO NOMINATE THE PROTECTOR OF THE SETTLEMENT. BUT DOES THE SETTLOR OWE FIDUCIARY DUTIES IN RELATION TO THIS POWER?

A typical Protector nomination clause might be:

"… the first members of the Board of Protectors shall be appointed by the Settlor by written nomination which may be revoked by the Settlor at any time or times during his lifetime … "

In *re the T Financing Trust* (a recent case in the Royal Court of Guernsey, which settled prior to final judgment), questions arose as to whether this provision imposed a *duty* to appoint, or a *power* to appoint, and if the latter, whether it was purely personal or fiduciary in nature. Since this form of wording did not impose any sort of obligation on the settlor, it became common ground that this was a power.

Whilst the members of the Board of Protectors, once appointed, clearly owed fiduciary duties in the manner in which they exercised their functions under the trust deed, it was submitted that the settlor was entitled to appoint as Protectors whoever he wanted, irrespective of their ability or objective appropriateness. (It was not, however, suggested that the settlor might emulate Caligula and seek to appoint a horse!)

The exercise of the power, whilst in a sense being undertaken on behalf of another (the trust/its beneficiaries), did not carry with it or give rise to a relationship by which trust and confidence were reposed in him, nor did it impose on the settlor any obligation of loyalty to any person or class of persons as to whether to exercise the power and if so how.

As against this, it was submitted that the Protectors had such an important role in relation to the trust that full and proper consideration

> "…it was submitted that the settlor was entitled to appoint as Protectors whoever he wanted, irrespective of their ability or objective appropriateness."

had to be given by the settlor to all relevant factors when making his decision, and it was suggested that the Court had the power to intervene if it had doubts about the process by which the nomination was made.

The correct approach to this question is to consider the construction, nature and scope of the power: if the function of a power is crucial to the proper running of the trust as a whole and for the welfare of the beneficiaries as a whole, or if a failure or refusal to act could jeopardise the proper administration of the trust, then it is likely that the power would be held to be fiduciary in nature. But it is suggested that the appointment of a Protector is not of itself crucial to the proper running of the trust.

RICHARD WALFORD acted for the principal beneficiaries in this substantial trust dispute.

Offshore trusts and the straightjacket of EU Law

RECENT YEARS HAVE SEEN HEIGHTENED TENSIONS ABOUT THE ENGLISH COURTS' PERCEIVED INTERFERENCE WITH JERSEY LAW TRUSTS. ONE CONTRIBUTORY FACTOR IS THE ENGLISH COURTS' DESIRE FOR ONE-STOP RESOLUTION OF DIVORCE AND ANCILLARY RELIEF CLAIMS. THE PERCEIVED NOTION THAT ENGLAND IS THE DIVORCE CAPITAL OF EUROPE MIGHT SUGGEST THAT THE PROPER RESPONSE IS TO SEND FORUM SHOPPING SPOUSES PACKING.

The UK's position as an EU Member State has, however, removed much of its power to control proceedings; owing to a range of European Regulations (not binding in Jersey). The so-called Brussels II *bis* Regulation ((EC) No 2201/2003) on jurisdiction in matrimonial matters *requires* an English court to entertain divorce proceedings in a very broad range of circumstances. Outside the context of divorce, the Judgments Regulation ((EC) No 44/2001) has been interpreted by the ECJ in an ever more literalistic way, which has progressively stripped the English courts of their powers to control forum shopping. They are, for instance: unable to stay proceedings brought against defendants domiciled in England, even in respect of foreign law trusts (*Owusu*); and largely powerless to prevent breaches of trusts jurisdiction and arbitration clauses in other Member States (*Gasser; Turner;* and *West Tankers*). This presents the English courts with the tightest of jurisdictional straightjackets.

Conversely, Jersey must compete against ever more extensive offshore firewall legislation designed to protect local law trusts. Indeed, no sooner had Jersey enacted new firewall legislation in Article 9, Trusts (Amendment) Law 2006, than the Guernsey legislature produced its own revised firewall provision (section 14, Trusts (Guernsey) Law 2007).

How might these tensions be bridged? In Jersey, whatever the legislation might say, there is an understandable reluctance to assist spouses who rely upon firewall provisions to escape their financial responsibilities. This has led to some creative interpretation of Jersey

legislation (*e.g. Re B; Mubarak*). In England, there have been nods in the direction of greater respect for Jersey trusts (e.g. the English *Mubarak* proceedings); but little real restraint in varying them. The English courts have, however, increasingly offset the strictures of their jurisdiction rules by referring to the need to have a "sideways look" (Wilson LJ in *C v C (Ancillary Relief: Nuptial Settlement)*) at foreign law in ancillary relief proceedings. And whilst the European tidal wave of private international law initiatives shows no sign of relenting, the UK has the option of not participating. Hence, the UK has not opted into the European Commission's recently proposed Succession Regulation (which might compel English courts to apply foreign rules of clawback in respect of Jersey law trusts) but will continue to participate in negotiations - in pursuit of a compromise that might reconcile its commitment to the European internal market with its relationship to offshore trusts jurisdictions.

PROFESSOR JONATHAN HARRIS is an editor of *Dicey, Morris and Collins, The Conflict of Laws*, advisor to the Ministry of Justice on the EU Succession Regulation and was instructed in *Charman v Charman* and *Mubarak v Mubarik*.

Chambers news

People

We are pleased to be able to announce that since our last Serle Speak Conor Quigley QC, a specialist EU law silk has become a tenant and Sir Mark Waller, former Vice-President of the Court of Appeal Civil Division, has joined our Alternative Dispute Resolution Panel as an arbitrator and mediator.

Conor was called to the Bar in 1985 and took silk in 2003. His practice covers all areas of European Union law, including State aid (in which he is regarded as a leading expert), competition law, public procurement law, tax law, and other EU-related aspects of commercial law.

Notable recent cases include *Louca v A German Judicial Authority*, one of the first judgments to be delivered by the UK Supreme Court, and *White v The Crown* in the Court of Appeal. He has been instructed in many important cases before the European Court of Justice and the higher UK courts, and has also represented clients in investigations and complaints before the European Commission and the OFT.

Sir Mark Waller was called to the bar in 1964 and took silk in 1979. He was a member of 1 Hare Court (which later merged with Serle Court) with a substantial commercial practice. He was appointed a Justice of the High Court (Queens Bench Division) in 1989, sitting mainly in the Commercial Court, being judge in charge of that court, before being made a Lord Justice of Appeal in 1996. He was Vice-President of the Court of Appeal Civil Division for four years before stepping down earlier this year.

We were also delighted that Christopher Stoner QC and Michael Edenborough QC were both successful in this year's Queen's Counsel appointment round; Christopher specialises in property litigation and sports disciplinary and regulatory matters and Michael practises in all areas of IP.

Directories

The 2010 Legal 500 directory was published in September and we have had another excellent year. As a set we are recommended in ten practice areas: Banking and finance, Commercial litigation, Company, Fraud: civil, Insolvency, Media, entertainment and sport, Partnership, Private client: personal tax, trusts and probate, Professional negligence and Property litigation. Individually we increased our recommendations again and now have an impressive 104.

We are extremely grateful to all our clients for recommending us so highly.

Awards

So far this year we have received nominations for Chambers of the Year at the Legal Business Awards and the STEP Private Client Awards. We have also been recognised again at the Chambers & Partners Bar Awards; Alan Boyle QC was named as Chancery Silk of the year and chambers was nominated for Chancery Set of the year.

Edited by Jonathan Fowles