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A trustee's top three

For those in the business of holding and managing private wealth, turbulence like we experienced in 2009 is the ultimate "stress test" for trusts. Weaknesses become apparent in existing structures, often requiring the structure itself to be amended. Investments perform badly and beneficiaries look for someone to blame. Tensions within the family or between various branches of the family become more acute. All of this leads to the development of the law and of drafting practice as practitioners and legislators adjust to changing requirements.

This article explores some of the common issues with which some trustees of Cayman Islands trusts have grappled recently, including those most likely to lead to disputes or to land the parties in court.

"Over-enthusiastic" drafting

Trust deeds which contain far-reaching no-contest provisions or clauses designed to eliminate altogether the beneficiaries' ability to access any information concerning the trust are destined to be fodder for future litigation. Ironically, rather than reducing the potential for litigation, this type of provision tends to increase it. It may only be a matter of time before the Cayman courts are asked to construe non-disclosure provisions. It is axiomatic that, when the trust fund is declining in value, beneficiaries are more likely to ask probing questions and to require supporting information, and so issues are more likely to arise.

The permissible scope of those clauses is likely to be only as wide as the extent to which it is possible to exclude (or indemnify in respect of) a trustee's liability, and for the same reasons. As a matter of Cayman Islands law, any attempt to exclude the trustee's core obligations or the beneficiaries' rights to enforce them, including the duty of good faith and to account to the beneficiaries for dealings with the trust assets, will be considered repugnant to the trust concept.

The leading Cayman Islands case on no-contest clauses is A.N. v Barclays Private Bank and Trust (Cayman) Limited[1]. The Chief Justice held that the no-contest clause had to be construed in the light of the irreducible core obligations owed by Trustees to beneficiaries and the beneficiaries' right to enforce those obligations. It could not operate so as to deprive a beneficiary of this right and therefore "must be read by implication as allowing not only such [beneficiary challenges] which are successful, but also [challenges] which are justifiable…".

The same could be said of clauses which attempt to restrict a beneficiary's ability to access trust information. Following the Privy Council's decision in Schmidt v Rosewood[2], it is clear that the Court is charged with supervising beneficiaries' access to information and documents as one aspect of its inherent jurisdiction to supervise the administration of express trusts. Such clauses are likely to be construed so as to preserve the beneficiary's ability legitimately to require, or a Trustee's obligation to provide, information and documents which are necessary in order to enable the beneficiary to enforce the core obligations, such as the Trustee's obligation to account.

Attempts to restrict a beneficiary's ability to access documents are likely to result in the first instance in a contested application for construction of the clause in question or for directions by a trustee because of the inevitable questions about the extent to which the clause can be upheld. Where matters are particularly time sensitive, the delay involved in approaching the Court may be time the parties cannot afford. The draftsman may attempt to narrow the clause so that information necessary to police the fulfillment of the core obligations may be obtained. However, this may not avoid the need for the Trustee to consider what information or documents fall within this category and what documents can legitimately be withheld on each occasion. Those very questions may in themselves give rise to issues requiring resolution by the Court.

There is, in any event, a clearer statutory path to achieving the same end under Cayman Islands law by the creation of a STAR Trust under Part VIII of the Trusts Law (2009 Revision). Pursuant to those provisions, a beneficiary of a STAR Trust does not, as such, have standing to enforce the trust, or an enforceable right against a trustee or an enforcer, so long as there is an enforcer with a right or a duty to enforce the trust. So far, there have been no reported cases of hostile litigation involving STAR Trusts. This may be, in part, due to the fact that the information flow to beneficiaries is more stringently controlled under the relevant statutory provisions.

[1] [2006] CILR 307
[2] [2003] 2 WLR 1442

Multiple fiduciaries

It is increasingly common for offshore trusts to include provisions creating the role of protector, or a protector by some other name. Often this is done by appointing a number of persons to form a management committee with extensive powers to direct the Trustee in relation to the management or administration of the trust property or to consent to the exercise of the Trustee's own powers. It is often said that this gives settlors a measure of comfort that someone will be involved in administering the structure who knows the family and its circumstances intimately and is able to give some direction to the more remote Trustee. However, the protector's role is often the issue most likely to lead to litigation in a typical trust. Introduce more than one protector or issues concerning the way a committee of protectors should function and one simply increases the likelihood that the administration of the trust will be plagued by issues about the functioning of the committee or the protector's exercise of his powers. Where the administration of the trust breaks down, this often only serves to multiply the issues that may ultimately have to be brought to the Court for resolution.

One such issue is the Trustee's ability to react quickly in order to take steps to preserve the value of the trust fund and react to changing markets where its ability to deal with assets depends on directions from a protector or committee of protectors. If the protector(s) delay unreasonably in responding to requests for consent or if the committee is deadlocked or affected by conflicts of interest, the administration of the trust may be paralysed at a time when the Trustee is required to act urgently. The Trustee may simply have no power to act until the issues are resolved.

The costs involved in seeking to resolve these issues by way of application to court can be significant. If there is a legitimate question of construction and all of the fiduciaries are acting in good faith and are necessary parties to any litigation to resolve the issue, they are likely to be entitled to have their legal fees paid out of the trust fund at the end of the day. The question whether the protector(s) should also be entitled to recovery of legal fees is often a thorny one, which may open up another battlefront.

Absence of suitable express powers

Flexibility and the ability to adapt to changed circumstances are integral to the efficacy of trust structures which are intended to last for successive generations. It is often the case, in particular with older trusts, that a Trustee finds itself unable to act quickly or efficiently to solve a problem affecting the trusts or to meet the needs or objectives of the beneficiaries because there is no suitable power available for the purpose or because such power as the Trustee has depends on consent from another party (usually a protector) and the necessary consent is being withheld.

Section 63 of the Trusts Law (2009 Revision)[3] allows the court to authorize trustees to engage in certain acts in the management or administration of the trust which are not otherwise permitted by the trust instrument or by law. The section cannot be relied on to alter the beneficial provisions of the trust in question[4] but it can also be useful where it is sought to empower trustees to partition funds held for the benefit of large families with multiple branches. Tax changes, global movement of beneficiaries and economic pressures often result in a desire on the part of various branches of the family to partition the fund so that they can go their separate ways.

In MEP and another v Rothschild Trust Cayman Limited and others (not yet reported, 20 October 2009), the Chief Justice made orders giving the Trustee power to divide the trust fund into three equal shares and to appropriate one share to each of three sub-funds nominated in the names of the three daughters of the primary beneficiary. Certain changes to the management and administrative provisions were proposed, but there were to be no changes to the beneficial interests beyond those which were necessarily incidental to the partition. The Chief Justice was satisfied that "the proposed division and partition of the Trust would be expedient for the better and more efficacious management and administration of the trust". Among other things, it would allow the Trustee to manage each sub fund with the particular needs, interests and desires of that branch of the family in mind.

Sara Collins
Partner

+1 (345) 814 7380
sara.collins@conyersdill.com

This article is not intended to be a substitute for legal advice or a legal opinion. It deals in broad terms only and is intended to merely provide a brief overview and give general information.

About Conyers Dill & Pearman

Conyers Dill & Pearman advises on the laws of Bermuda, British Virgin Islands, Cayman Islands, Cyprus and Mauritius. Conyers' lawyers specialise in company and commercial law, commercial litigation and private client

[3] which provides that "Where in the management or administration of any property vested in trustees, any…transaction is in the opinion of the Court expedient, but the same cannot be effected by reason of the absence of any power for that purpose vested in the trustees by the trust instrument, if any, or by law, the Court may, by order, confer upon the Trustees…the necessary power".

[4] Such variations to the beneficial entitlements can be achieved by way of compromise of a genuine dispute or under the court's statutory jurisdiction, under s. 72 of the Trusts Law, to approve variations on behalf of minor, unborn or unascertained beneficiaries, which will then take effect if all adult beneficiaries have also consented.

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For more information please contact:
Naomi Little
+1 (441) 298 7828
naomi.little@conyersdill.com
www.conyersdill.com