

RECEIVERS AND REVOCABLE TRUSTS: RESERVED POWERS CANNOT BE EXERCISED AGAINST THE WILL OF THE SETTLOR

Nigel Meeson QC – October 2009

Update: Court of Appeal upholds the decision of the Chief Justice of the Cayman Islands

In a previous case note the judgment of the Chief Justice of the Cayman Islands in *TMSF v Merrill Lynch Bank and Trust Company (Cayman) Limited and others* was considered. This decision dealt with a settlor's power to revoke a trust and a judgment creditor's ability to enforce that power of revocation through means of appointment of receivers by way of equitable execution. The Chief Justice held that a receiver could not be appointed because the power of revocation was not property.

The ruling was appealed to the Cayman Islands Court of Appeal (Chadwick P, Mottley & Vos JJA) who dismissed the appeal on 18th September 2009. The judgment of the Court was given by Vos JA.

The background to this case was that the Plaintiff (TMSF) obtained a default judgment against Mr. Demirel in the Grand Court of the Cayman Islands in the sum of US\$30 million in an action to enforce a judgment which they had obtained against him in Turkey. In 1999 Mr. Demirel had established two discretionary trusts by separate deeds in which he was both the settlor and a beneficiary. Both trusts contained reserved powers to the settlor inter alia to revoke the trusts. TMSF sought to have the court appoint a receiver by way of equitable execution over the judgment debtor settlor's power of revocation so as to enforce the Cayman Islands judgment.

As explained in the previous case note, the emphasis of the reasoning of the Chief Justice had been upon the fundamental legal distinction between power and property. Although the judgment of the Chief Justice was described by Vos JA as "lengthy and incisive" the emphasis of his own reasoning was rather different.

Vos JA stated that the appeal raised two issues. First, whether as a matter of law the court has jurisdiction to appoint receivers at the behest of a single judgment creditor, by way of equitable execution, over a power of revocation in a trust. Secondly, whether, if such jurisdiction did exist, the court ought to exercise its discretion to appoint receivers over the powers of revocation in Mr. Demirel's trusts. It was the first issue which was the most significant and the Chief Justice had held that there was no jurisdiction. The Court of Appeal agreed.

Vos JA began by an analysis of the proper construction of the powers of revocation in the two trusts (which were in identical terms). The relevant powers were in the following terms:

"This trust may be revoked, amended, varied or altered in any manner whatsoever from time to time and at any time by the Settlor by deed delivered to the Trustees provided always that no such revocation, amendment, variation or alteration shall take effect until actual receipt of the instrument by the Trustees or with the written consent of the Trustees thereto if such revocation, amendment, variation or alteration would increase or extend the obligations, liabilities or responsibilities of the Trustees."

Vos JA was critical of drafting of this provision which he considered confusing but nevertheless concluded (as had in fact been common ground between the parties) that the

power of revocation was unfettered in that it could be exercised without anyone else's consent.

Vos JA premised his reasoning on the main jurisdictional issue raised in the appeal on the following, further distinction: whether, on the one hand, a power of revocation should, at common law or under various statutes, be regarded as a chose in action and thus property; and, on the other hand, whether as a matter of policy, the courts should recognize for the first time that equitable execution can be allowed in respect of powers of revocation of the kind in issue between the parties. He held that the former question, even if decided in favour of TMSF, would not determine whether it is appropriate to allow equitable execution over that species of property. He considered the question of allowing equitable execution over powers of revocation as a policy question to be decided using the principles explained by Lawrence Collins L.J. in the matter of *Masri v Consolidated Contractors International SAL*¹ as a starting point.

This approach differed from the approach of the Chief Justice who had started with the logically prior question of whether the power of revocation could be regarded as property because if it could not then one never reaches the policy question. Although Vos JA was of course correct that the property question would not necessarily be determinative of the outcome, upon analysis neither would the policy question. One can only conclude that because the outcome of the policy question appeared very clear to the Court of Appeal they were in fact seeking a short cut which avoided considering the property question.

The policy issue was therefore whether a power of revocation should be available to a single creditor by way of equitable execution, so as to enable that single creditor to procure its execution and to recover all the settled assets of the trust to satisfy its judgment debt. In agreeing with the learned Chief Justice, the court held that if such an advance in the law was to be made, it should be the legislature to whom the task fell and not the Courts.

Although Vos JA expressed his own reasoning as being premised on policy considerations, his reasoning effectively mirrored that of the Chief Justice who considered same the question as being answered by a distinction between power and property.

Central to both the analysis of the Court of Appeal and of the Chief Justice was the old authority of *Thorpe v Goodall*² and its legislative follow up. In *Thorpe v Goodall* Lord Eldon had said that the Court did not have power to compel a bankrupt to execute a general power of appointment over trust property in favour of his creditors. The law was altered shortly afterwards to introduce the concept which later became section 44 of the English Bankruptcy Act 1883 and section 100 of the Cayman Islands Bankruptcy Law (1997 revision) so as to enable such a power to be exercised by the trustee in favour of the bankruptcy estate.

Both courts pointed to the fact that in the law of bankruptcy, specific legislation had been required in order to make a general power to be considered as property passing to the trustee in bankruptcy. Therefore, both courts in effect held that all legislative enactments which included powers in the definition of property had been so enacted so as to make it clear that the Legislature had considered the particular context of that power and had decided that, for that specific context, property would include general powers, exercisable by donees in their own favour. Neither court was able to find any distinction between a general power of appointment and a power of revocation, the latter being merely a narrow power of appointment.

However, whereas the Chief Justice had considered that these authorities and legislative enactments showed that a power was not property, the Court of Appeal proceeded down the avenue of policy, finding that it would be unwise and inappropriate for a court to allow equitable execution over a power of revocation by means of the kind of incremental advance envisaged by Lawrence Collins L.J. in *Masri supra*. It reasoned that where legislatures had taken it upon themselves for 200 years to decide when powers should be considered to be

¹ [2008] EWCA Civ 303

² (1811) 17 Ves. 388, 460; 1 Rose 40

included in the definition of property, the court should assume that the legislature would not wish judges to arrogate themselves that decision, especially in situations where the legislature had not yet seen fit to do so.

Therefore, in agreeing with the learned Chief Justice's findings, the Court held that the incremental advance in the availability of equitable execution to include powers should, as a matter of policy, await express legislative intervention.

The Court of Appeal did, however, expressly disassociate itself from the learned Chief Justice's statement that the extension of jurisdiction sought would "strike at the very heart of the trust concept", commenting that conceptually, there is little difference between including such powers in a bankrupt's estate divisible amongst his creditor's and including them in the species of property over which equitable execution is available. With respect to the Court of Appeal it seems that this implicit criticism may be misplaced. The context in which the Chief Justice had said that the extension of jurisdiction would "strike at the heart of the very trust concept" was in recognizing, as the Chief Justice put it, "the far reaching implications of policy" that is carried with an extension of the jurisdiction. In essence this is no different to the Court of Appeal's own recognition that the policy extension could not be carried out judicially, but required legislative intervention.

In a further *obiter* remark Vos JA disagreed with the learned Chief Justice's example, in this context, of a settlement in favour of an incapacitated child by which capital or income can be appointed for his or her benefit but with a power of revocation reserved to the settlor with the intention that he only exercise it if the child predeceased the settlor. Vos JA stated that if equitable execution were available as a matter of law, the court would, in such a case, refuse to exercise its discretion to allow equitable execution over a power of revocation in such a trust. The suggestion that the exercise of the Court's discretion (if it had had one) may depend upon the worth or the appeal of the beneficiaries of the trust, or an investigation of the mind or unexpressed intention of the settlor is a troubling one, and with respect this would be an issue upon which rather more reasoned analysis may be required.

The fundamental point common to the judgments is that, in the case of bankruptcy, legislation has provided that a power of revocation or a general power of appointment may be exercised to cause the trust assets to be available in the collective bankruptcy process in favour of the general body of creditors of the bankrupt. If legislation was required to do this in the case of bankruptcy, then plainly legislation is required if an individual creditor is to be enabled to bring about the end of a trust by the forced exercise of a general power of appointment or power of revocation.

Whether one focuses as the Chief Justice had done on the distinction between power and property, or whether one focuses on the policy issue as the Court of Appeal did, the result is the same.

Conclusion

The Appeal Court's decision should be welcomed by trusts practitioners in that it recognises that the existence of settlors' reserved powers should not expose trust assets to attack unless specifically determined by the legislature to be appropriate and in the public interest to do so.

Nigel Meeson QC is head of litigation in the Cayman Islands office of Conyers Dill & Pearman and appeared on behalf of the successful Settlor in this appeal.

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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.

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