In depth

Disputes over trusts that hold corporate structures

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Abstract

This article considers two important issues that arise where, as is commonplace, trusts own corporate structures. The first is the extent to which the running of such companies can be left by the trustee to the directors through the use of an 'anti-*Bartlett* clause'. The second is when the trustee can obtain information about the running of the companies. Both areas have been the subject of recent offshore case law, and the article analyses these developments.

Introduction

1. As a matter of law, the starting point is that a company by a trust is just another asset.

2. However, companies owned by trust pose unique issues because—at least where the company is more than just a pocket for an asset—they are often intended to be the place where in practice the structure is run from, rather than—as is the case under classical trust law—the trust level of the structure.

3. We shall deal with two of these issues that have been the subject of recent litigation, namely:

i. when the running of the company can be left to the directors through an 'anti-*Bartlett* clause' that attempts to negate the ordinary *Bartlett v Barclays Bank*[1] duty on the trustee to involve itself with the company like any other asset of the trust,[2] and
ii. when the trustee can obtain information about the running of the companies.

Anti-*Bartlett* clauses and their proper limits

4. Anti-*Bartlett* clauses are often lumped in with exclusion clauses as devices to avoid trustee liability. This brings out the practical importance of evaluating their proper limits, something that the cases that we have come across have not yet had to grapple with. This section attempts to do that. The central submissions are that:

i. such clauses are different from exclusion clauses in important respects, and that one must take that into account when considering their validity and proper limits, but
ii. one must be very careful
iii. that they are worded correctly to achieve their purpose (particularly in light of the *Citco* judgment mentioned below); and
iv. not to remove their protection by interfering in the companies, and there remains a lingering question over their validity.

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1. [1980] 2 WLR 430.
2. This part of the article is written by Jonathan Hilliard and the second half by Andrew Child.

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The good sense of anti-Bartlett clauses

5. The well-known starting point is that in the absence of contrary provision in the trust instrument is that a trustee owes a duty of care to supervise trust-owned companies as much as other trust assets.

6. However, in a number of important practical respects trust-owned companies are not the same as other trust assets.

7. First and foremost, there will normally be one or more family members associated with the trust running the company.

8. Secondly, those persons will often be best placed to run the company.

9. Thirdly, the trustees will normally not have the skills in the relevant industries to run the company.

10. Fourthly, the motive for placing the company into trust, whether it be tax-driven, for asset protection or for succession planning, does not of itself mean that it makes sense from a practical perspective for the running of the company to be significantly disturbed or altered as a result of the asset being placed into trust.

11. Fifthly, if the trustees were to exercise a hands-on supervisory role, there would be a duplication of cost with those running the company.

12. The above facts bring out the point that the purpose of an anti-*Bartlett* clause is to *delimit the responsibilities* of those involved with the trust. It makes clear that the responsibility for running the company lies with the relevant family members, and thereby avoids duplication of effort and cost. This is very different to an exclusion clause, because that is a clause excluding liability for something which the trustee has a duty to do and therefore for which he has a responsibility.

13. One gets a good sense of this from a recent Hong Kong Court of Appeal case called *Highmax Overseas Limited & others v Chau Kar Hon & another,* 21 May 2014. In that case, an individual had set up a number of property-holding companies and transferred properties into them, then transferred those companies into trust. The individual then went bankrupt and his trustee in bankruptcy sought to set aside the transfer of the properties into the companies, which—if successful—would obviously have meant that the shares in the companies held in the trust would become worthless. The trustees brought a *Beddoe* application seeking guidance as to how it should conduct itself in the proceedings, and the basic message from the Court was that this should be left to the company. The company's directors were the people who should be taking this decision, not the trustee shareholders.

The limits and validity of anti-Bartlett clauses

14. I will consider five means of attacking or circumventing anti-*Bartlett* clauses.

15. The first and obvious point is to avoid drafting an anti-*Bartlett* clause in a way that makes it obviously invalid. Therefore, it is important not to exclude in an *unqualified* manner responsibility in relation to the trust-owned company or this could make the clause invalid as an attempt to avoid trustee accountability entirely. It is better to have a clause that makes clear that the trustee's duties will be engaged in certain circumstances, such as where it has actual knowledge of company mismanagement.

16. The second route is argue that it has been inserted in circumstances that makes it invalid, seeking to rely on the suggestion in *Bogg v Raper* (8.4.98 CA) that there can be situations where a trustee cannot rely on an exclusion clause by virtue of the circumstances in which it was inserted. Therefore, it is important to start by looking at *Bogg*.

17. In *Bogg*, it was argued that solicitor trustees of a will trust were taking a benefit from the trust by inserting an exclusion clause so that the fiduciary 'no profit' rule applied, meaning that the onus shifted to the solicitor to show that the settlor had received full and independent advice as to the presence and terms of the exclusion clause. The Court of Appeal rejected this argument, holding that the clause did not confer a benefit on the trustees but instead delimited the extent of their liabilities. However, it hinted that if the solicitor trustees knew that the settlor was unaware of the clause and/or its terms, matters might be different.

18. It is suggested that an anti-*Bartlett* clause is even further from a clause conferring a benefit on trustees. It is a clause that sets out the differing responsibilities of trustees and family members. Furthermore, it is a clause that the settlor is likely to be aware of because the economic settlor will often be one of the persons involved in running the company, and therefore unlikely to expect or want the trustees second-guessing his business decisions. Therefore, it is suggested that the room for challenging the inclusion of an anti-*Bartlett* clause is even less than an exclusion clause. As for the hints in *Bogg* about what the position might be if the trustees knew that the settlor was not aware of the terms of the clause at the time of its insertion, those should probably be read in the context of *Bogg*, which concerned the terms of the will and therefore (as the Court of Appeal made clear) the ordinary knowledge and approval requirements for a will would apply. In any event, it is suggested that this fact set is relatively unlikely to occur in an anti-*Bartlett* case, for the reasons set out above.

19. The third route is to argue that the trustees *have* interfered in the running of the business, so that they cannot rely on a clause allowing them not to become involved. I shall return later to the circumstances under which a trustee will be said to have done this, but appointing trustee officers to the company boards is an example.

20. A fourth and very important possible route has been opened up by the 2014 BVI decision in *Appleby Corporate Services (BVI) Limited v Citco Trustees (BVI) Limited*, 20 January 2014, which is to argue that there was a failure to *monitor* the company and say that this is something different from a failure to *interfere* in the company.

21. Many anti-*Bartlett* clauses are along the following lines, which are taken from paragraph 8 of the Schedule to the BVI Trustee Act:

> *THE Trustees shall not be bound or required to interfere in the management or conduct of the affairs or business of any company in which the Trust Fund may be invested (and whether or not the Trustees have the control of such company) And so long as no trustee of this instrument has notice of any wilful negligence wilful default or fraud or dishonesty on the part of the directors having the management of such company they may leave the same (including the payment or non-payment of dividends) wholly to such directors And no beneficiary is entitled as such beneficiary in any way to compel control or forbid the exercise (including in any particular manner) of any voting or other rights at any time vested in the Trustees with regard to such company including without prejudice to the generality of the foregoing any powers the Trustees may have (even if also directors of such company) of compelling such company to distribute any dividend. (emphasis added)*

This was the clause under investigation in *Citco*.

22. Some clauses are longer and expressly refer to there being no duty to *enquire* into the conduct of the company as well as being no duty to interfere, or even go further and say that the trustee *shall* not monitor. An example of the former is:

> *The Trustees are under no duty to enquire into the conduct of, or obtain any information regarding, a company in which they are interested and, unless they have actual knowledge of circumstances which call for enquiry, they may assume at all times that the business of any such company is being conducted diligently in their best interests and that all information received is accurate and truthful.*
>
> The Trustees shall not be bound to exercise any control they may have over or to become involved in the conduct of the business of any company. The Trustees may leave the conduct of such business to the persons authorized to take part in the conduct thereof and shall not be bound to supervise them as long as the Trustees have no actual knowledge of any dishonesty relating to such business. (emphasis added)

23. The facts of *Citco* were slightly unusual for a combination of two reasons:

a. the company owned by the trust simply held investments rather than being a family business of any kind, and

b. the trustee botched the investment agreement so that it said that the *trustee* and the company engaged the services of the investment manager to look after the company's investments and that the investment manager was subject to review by the *trustee* and the company.

24. There are two key passages in the judgment, of which the second is the more important.

25. The first is paragraph 30, where Bannister J explains that the fact that the intention of those transferring the companies into trust that the companies would continue to be managed as before, which was termed a 'pre-pack arrangement', does not automatically mean that the trustee can leave this state of affairs in place. The trust framework places duty on the trustee to concern himself with the trust's investment, unless this is excluded.

26. That is correct and straightforward. However, the second point is that it was held at paragraph 33 that the fact that the anti-*Barlett* clause removed the obligation to *involve* itself in the *management* if the company:

> *did not relieve it of the duty to satisfy itself from time to time that nothing untoward was affecting the value of the shares. They are two different things.*

27. This is not a million miles from the (if anything slightly harsher) comment in the first Law Commission paper on the topic, LC171 (2002), which stated at paragraph 4.91:

> *In some cases, a trustee will be unable to rely upon duty exclusion clauses as a matter of construction of the particular clause. For example, the terms of a trust may provide that the trustee shall not be obliged to supervise or interfere in the management of any company in which he holds the majority shareholding. This duty exclusion clause does not prevent the trustee from supervising or interfering in the management of the company. It does mean that the trustee who fails to supervise or to interfere is not automatically in breach of trust. But if the failure to supervise amounts to negligence on the part of the trustee, the duty exclusion clause should not save the trustee from liability. A trustee who fails to exercise a power when he or she should do so commits a breach of trust. In this example, liability is incurred by the trustee without any need to strike down the duty exclusion clause. As a matter of construction, the clause does not apply where the trustee has acted negligently.*

See also Appendix D paragraph 18 of the final report LC 301 (2006):

> *We prefer the interpretation that type 2 duty modification clauses address only the implied duty to do a particular thing and do not affect the underlying powers to act. This position accords with the basic principles of trust law and is, to some extent, acknowledged by the widespread use of simple duty modification clauses supported by liability exclusion clauses.*

28. In *Citco*, the manager stepped well outside the investment guidelines, in a way that should have been obvious from the reports submitted up to the trustee, so it was held that the trustee was in breach of its duty and liable for the decrease in the trust fund that resulted.

29. What can we take from this? At a general level:

1. According to the BVI Court, there is a duty of periodic monitoring according to BVI court.
2. And as part of this the trustee must satisfy itself that nothing untoward was happening at the company level.
3. But this is different from interfering in management.
4. So there is some supervisory duty that remains.

30. However, when we move from the general principles to what this means in practice, the decision raises important questions, in particular, when one examines what the trustee can be expected to do by way of monitoring. *Citco* was an easy case because the trustee signed up to the investment management agreement, the investment manager's role was subject to the review of the trustee and the trustee received regular reports.

31. However, the trustee has therefore involved himself in the investment by signing up to the management agreement for management of the company's investment and retaining an oversight role. Therefore, the case could have been decided on the more orthodox ground that the trustee *had* involved himself in the management of the company's investments in that way, so could not be heard to say that he had stood back.

32. Or one could have said that the manager's conduct was getting pretty close to 'wilful negligence' and therefore the trustee had notice of this so that the clause does not apply on its own terms.

33. However, finding that the clause is intended to leave a monitoring obligation in all cases, as Bannister J's words taken literally do, is more difficult:

1. If the trust holds a family trading company, monitoring means taking active steps to obtain information, potentially involving changing articles so as to get information as to the running of the company.[3]
2. How can a trustee without any professional skills in the business of the family company monitor its performance so as to work out whether something untoward is going on?
3. Is it intended that the trustee should incur the not inconsiderable costs of the sort of role in (2), which would be considerably greater than the costs in *Citco* of just checking that the investment guidelines had been complied with?

34. Another view is that the purpose of the clause is that it is intended to exclude the monitoring obligation, for this precise reason. 'You needn't interfere' is intended to mean you need not interfere *to monitor or to actually take steps to run the business.*

35. However, the lesson of *Citco* appears to be that if you want to exclude the monitoring obligation, you are going to need to use clearer language.

36. This leads into the final route for attacking anti-*Bartlett* clauses that do purport to exclude the monitoring obligation, which is to argue that they are invalid by trespassing on the core content of trusteeship. The danger here is that if you try to draft away the monitoring obligation, you may invalidate the whole anti-*Bartlett* clause and thereby actually place the trustee in a worse position.

37. This is an argument adverted to by the Law Commission and Professor Hayton.

38. In my opinion, such clauses should be treated as valid. It is certainly true that there is a legitimate concern that allowing *any* duty to be excluded would strike at the heart of the trust. However, there are good reasons for anti-*Bartlett* clauses, and therefore correspondingly it is suggested that one should be reluctant to strike them down when (i) they only apply to certain trust assets and (ii) there remain (a) duties on the directors to run the company properly and (b) some level of oversight, however, small, on the trustees, by virtue of the obligation to interfere if wrongdoing comes to their attention. Moreover, the Trustee Act 2000 does suggest that it is possible to exclude the trustee's duty of care (Schedule 1 paragraph 7).

39. A compromise solution is that suggested by Professor Hayton, which is that such clauses should not be allowed to a *very low level* supervisory duty. In other words, there may be situations where the trustees do not quite have actual knowledge of dishonesty, but the situation is so crying out for enquiry that no reasonable trustee could sit back and fold his hands. Such a solution says that there is not a periodic monitoring obligation, but circumstances may arise where the trustee has to do something even if the anti-*Bartlett* clause may suggest to the contrary.

40. Other possible routes for dealing with the problems thrown up by *Citco* are as follows:

1. Use a statutory regime which expressly removes these sorts of duties, like the BVI VISTA trust regime (or seek to use the STAR Trust regime so as define the purposes of the trust in a way that achieves the same effect);

3. See the discussion in Toby Graham, 'Disclosure of Documents of Trust-Owned Companies: Is Butt Broke?' (2012) 18 Trust & Trustees 700–17.

2. Give the settlor the right to issue investment directions to the trustee. However, this will likely make the settlor's powers fiduciary and the question remains of whether the Court will want the trustee to continue to have some sort of supervisory duty to check the appropriateness of the directions.

41. Fifthly and finally, one can try to circumvent an anti-*Bartlett* clause by seeking to attack the decision of the directors of the company owned by the trust, by seeking to bring about an action on behalf of the company in question against its directors. To do this, the beneficiary will either need to seek to bring a derivative action on behalf of the company or seek to force the trustees to bring about such a claim.

42. One interesting aspect of this question is whether a beneficiary claimant can shortcut the need for the company to bring the claim by bringing an unlawful means conspiracy claim himself directly against the directors of the company, relying on the breach of the directors' duties to the companies as being the unlawful means. On one hand, a breach of the directors' duties is unlawful means, but on the other, the victim of that breach is the company, rather than the beneficiary of the trust.

The use of linked employees

43. One of the routes mentioned above that often causes problems in practice is the third route (paragraph 19 above), which is the use of persons associated with the trustee to manage the underlying companies, and the question of whether the trustee will be thereby taken to have involved itself with the running of the companies such that it cannot rely on the anti-*Bartlett* clause.

44. One possible analysis is as follows:

1. The mere fact that the directors come from a source associated with the trustee, such as a law firm that is associated with or owns the trustee, is not itself sufficient to mean that the trustee have involved itself with the running of the companies. For example, a partner of a solicitor's firm is not part of the trustee just because his firm sets up a trustee company and his knowledge should not be attributed to the trustee.
2. However, if the individual is an employee of the trustee, matters are more problematic because there is a strong case for attributing his actions to the trustee.
3. It is also important to set up proper reporting lines, so that the companies report up to the trustee in a way that makes clear that they are separate persons.

Obtaining information in relation to companies owned by trusts

45. *In the matter of the R and RA Trusts* is a Guernsey Court of Appeal decision concerning the obtaining of disclosure of information by a trustee from beneficiaries of the underlying trust fund.

46. The background to the application was that the trustee proposed a partition of the interests in the trust fund, with a view to separating out the beneficial interests of the daughter from her brothers and mother.

47. The daughter had already received an interim appointment of £22 million in 2009 by way of payment on account to the W Trust (a trust set up for the benefit of the daughter and her children).

48. The trustee instructed an Advisory Firm to undertake an independent and up to date valuation of the trust assets with a view to a further appointment to the daughter in final partition of her interests.

49. The Advisory firm reported that they required various further information to finalize their valuation and that it was believed that such information was in the hands of the beneficiary brothers.

50. The trustee therefore issued a two-stage application before the Guernsey Court (1) seeking disclosure of information regarding the trust assets from the beneficiaries with a view to (2) upon receipt of a satisfactory valuation of the trust assets seeking the blessing of the Court for a partition, the proposed

partition being a 'momentous' decision (category 2 *Public Trustee v Cooper)*.

51. The trust Assets consisted of (i) an Investment Portfolio, (ii) a London Property Portfolio, (iii) an Africa Property Portfolio, and (iv) Business interests in Africa.

52. The information required by the Advisory Firm focused on two areas:

i. Virtually, all the liquid assets of the trust fund had on the advice of the younger brother been place in a BVI Investment Company which sustained a significant drop in value ($44 million) in 2011. The Advisory firm had been investigating reasons for the drop in value but considered they had not received satisfactory information or explanations from the younger brother.
ii. Concerns also arose concerning a large loan of $171 million (the F loan) ostensibly made by a company F Limited to one of the Trusts as evidenced by two promissory notes executed in 2006. A question arose as to whether the loan was actually enforceable or whether in reality it had been used as a means of contributing capital to the Trust, it being believed that F Limited was wholly owned by the S Trust, of which mother and sons were beneficiaries, but the daughter was not.

53. The decision by the Deputy Bailiff at first instance held that the orders sought by the trustee were not against the sons in their capacity as beneficiaries but rather as persons who were advisors to various companies within the trust structure. Making the orders sought would not promote or vindicate their positions or interests as required by Jersey Court of Appeal case *BCD Settlements*.

54. The trustee having received a judgment at first instance declined to pursue an appeal, relying on *Re Londonberry Settlement*:

> *This appeal, as it seems to me, is an irregularity. Trustees seeking the protection of the court are protected by the court's order and it is not for them to appeal. That should be done by a beneficiary. . .. (Harman LJ).*

55. The trustee in so doing ignored the contrary view of Salmon LJ in *Re Londonberry*, namely:

> I agree with what has fallen from my Lords. However, in my view the trustees were fully justified in bringing this appeal. Indeed it was their duty to bring it since they believe rightly that an appeal is essential for the protection of the general body of beneficiaries. (Salmon LJ).

56. The daughter therefore was left to pursue the appeal on her own.

57. The Guernsey Court of Appeal were critical of the trustee's approach:

> In my judgment, the view of Salmon LJ is to be preferred. Whilst I fully accept that in the majority of cases a trustee who has sought directions from the court should not appeal even if he is not convinced that the court has reached the right decision, a trustee is perfectly entitled to appeal if convinced that the decision of the court is not in the best interests of the beneficiaries. (Sir Michael Birt).

58. The Guernsey Court of Appeal cited *Alhamrani v J P Morgan Trust Company (Jersey) Limited* 2007:

> Strictly speaking, a trustee who appeals may be at risk of an adverse costs order should the appeal fail; but such an adverse costs order will only be made in administrative proceedings where the appeal court concludes that the trustee has acted unreasonably in appealing, because it is only where a trustee has acted unreasonably that he is deprived of his indemnity as to costs. (Vos JA)

59. Sir Michael Birt concluded:

> In my judgment, given that they clearly believed – and still believe – that the information sought on the application is important for them to reach a fair conclusion as to the division of the assets of the Trusts, the Trustees should have taken on the responsibility for appealing in this case. Even if, contrary to the above, the initial appeal was to be left to the daughter, they

> should . . . have actively supported it if they believed that the best interests of the beneficiaries as a whole would be served by the information being provided.

60. The Hon Michael Beloff QC agreed:

> On the ancillary issue as to the Trustees' entitlement to appeal a decision of the kind before us. I am in the Salmon rather than the Harman camp.

61. The appeal gave rise to the following issues:

i. Should *BCD Settlements* be followed in Guernsey?
ii. Does Section 69 of the 2007 Law permit the Court to order a beneficiary to provide information to a trustee in relation to a trust?
iii. Assuming the Court has jurisdiction to make the order requested, should it do so on the facts of the case?; and
iv. If the court does not have jurisdiction under section 69, may it order disclosure under Part(X)(Rule 71 in particular) of the Royal Court Civil Rules 2007 (RCCR)

62. The Trusts statute in Guernsey was accepted by all to be similar to that of Jersey under which *BCD Settlements* had been decided. Section 69 of the Guernsey 2007 Law read:

> On the application of [a trustee] or [a beneficiary], the Royal Court may
> (a) make an order in respect of:-
> (iii) a beneficiary.

63. Similarly Article 51 of the Trusts (Jersey) 1984 Law read:

> The court may if it thinks fit:-
> make an order concerning
> (iii) a beneficiary

64. The judgment of *Re BCD Settlements* outlined the approach of the Jersey Court Appeal in construing their statute:

i. it is clear that some limit must be imposed on the width of the jurisdiction conferred by the article;
ii. it would not be permissible to regard the article as providing a source of jurisdiction to grant relief where no other cause of action existed merely because the defendant happened to be a beneficiary under some trust.;
iii. it is clear that the power to make an order concerning a beneficiary is confined to cases where the order affects the beneficiary in his capacity as such – that is to say, in his capacity as beneficiary of the trust whose administration the court is supervising. The foundation of the jurisdiction lies in the nexus between trustee and beneficiary arising out of the trust relationship; and
iv. The fact that a person is a beneficiary is not of itself sufficient to justify the making of an order: the order must be made for the purpose of vindicating, or at least promoting, some right or interest arising directly out of the trust relationship.

65. Having analysed *Re B, C and D* Sir Michael Birt in the leading judgment of the Guernsey Court of Appeal made a number of observations:

i. It is not entirely clear whether, when it refers to the order in that case falling outside the 'scope' of Article 51 or 'beyond the proper limits of the jurisdiction' or being concerned with 'how the undoubted limitation on the power is to be identified' the Court of Appeal was referring to the *jurisdiction* (i.e the power) to make the order in question or to the circumstances in which it would be proper for the Court to exercise the theoretical jurisdiction which it had.;
ii. If the Court was intending to say that there was simply no jurisdiction (in the sense of power) to make the orders in that case, I would respectfully disagree;
iii. I think it more likely that the Court was pronouncing that notwithstanding the wide theoretical jurisdiction, the Court must exercise that jurisdiction on a sensible and principled basis. I entirely agree with that sentiment.
iv. Nevertheless, in my respectful judgment, the Court in BCD articulated too rigid a test. It is always difficult to

envisage future circumstances until they arise and how words in a judgment may apply to such circumstances. The danger is that a judgment is construed as a statute. Indeed that is what has occurred here.

66. Considering the facts of *R and RA Trusts*, the Guernsey Court of Appeal adjudged that disclosure was both possible and appropriate to order:

i. I accept without reservation that it is likely to be extremely rare for a court to order a beneficiary to provide information to a trustee, let alone another beneficiary. In general terms, a beneficiary does not owe any duty to a trustee, so that the considerations which lead a court to order a trustee to disclose the information to a beneficiary do not arise in the reverse situation. Nevertheless, I do not accept that the Court may not do so where it is satisfied that such an order is in the best interests of the beneficiaries.
ii. In summary, whilst fully accepting that a beneficiary does not owe a fiduciary or other duty towards a trustee ... nevertheless, if the Court concludes that the provision of information by a beneficiary is required in order to protect the interests of the beneficiaries as a whole, it is my opinion that the jurisdiction conferred by Section 69 and the inherent supervisory jurisdiction of the Court in relation to trusts are both wide enough to encompass such an order.

67. Whilst, however, the Court of Appeal was willing to permit disclosure under the substantive Trust law, it was not willing to order disclosure pursuant to the relevant Guenrsey Civil Procedure Law, Part X (Rule 71 in particular) RCCR 2007:

i. It is important to keep these two procedures separate as considerations which will influence the Court as to whether to order disclosure are very different. In the case of an application under the trust supervisory jurisdiction, the question is what order should be made having regard to the interests of the beneficiaries, the duty of the trustee to account, matters of commercial confidentiality and many other aspects alluded to by Lord Walker in *Schmidt*. Conversely, in the case of ordinary litigation, the test for disclosure is whether the documents are relevant (or possibly relevant) to the matters in dispute between the parties.
ii. In my judgment it is not possible for a beneficiary or trustee to bring a stand-alone application for disclosure in relation to a trust and then seek to argue that, because this is being opposed, there is an issue between the parties and the Court can use its power under RCCR.

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