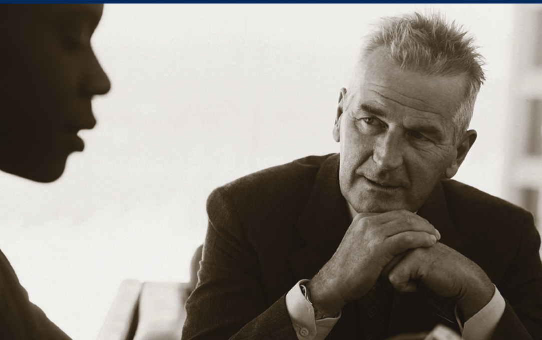

Contentious aspects of modern trusteeship

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There is no doubt that trust disputes have increased over the last few years, whether they be claims from disgruntled beneficiaries, attacks as to the validity of the trust, claims regarding the investment performance, attacks from creditors or disputes involving marital breakdown.

It is perhaps not surprising that disputes have increased. We have seen over the last 20 years or so increased globalization of families and hence international tax issues to take into account, increasing complexity of the assets held in trusts, a worldwide financial crisis, significant changes to legislation governing trusts, ever changing tax rules, as well as the introduction of a raft of regulation.

Professional trustees have therefore needed to up their game significantly in order to ensure that they properly address the potential risks in dealing with the administration of trust structures. We will touch on some of the contentious aspects of trusteeship which we encounter (and suggest ways to mitigate them) and in doing so we will draw on our experience both from an English and Guernsey law perspective.

Whatever the genesis of a dispute, we believe it is always beneficial (but not always possible) to avoid litigation. It has been said:

"Litigation is like firing an antique blunderbuss; difficult to aim, unsophisticated and the user is never absolutely sure that it is not going to blow up in his face. Only to be used with trepidation. However, if its the only thing you've got between you and an enraged bull elephant, use it quickly! The trick is making sure it is not the only thing you've got" (Russell Clark, Carey Olsen).

Prevention rather than cure

While it is important at the onset of a dispute that the trustees take appropriate advice, identify the type of dispute and take whatever appropriate

continued...

steps it can to resolve the dispute, it is perhaps more important that trustees conduct themselves in such a way as to assist in preventing disputes from arising in the first place. Steps which can prevent disputes arising (or at the very least assist the trustees in addressing the dispute) revolve around the quality of the administration activities from the very outset and throughout the trust period:

1) Establishing the trust

First, the trustees should ensure that the trust is validly created, the settlor's reasons for creating the trust are well understood and that the trust's terms are appropriate to meet the objectives of the settlor.

a) Validity

Although obvious, it is critical to ensure that the three certainties, namely; certainty of intention, certainty of subject matter and certainty of objects, are all present if the trustees wish to prevent attacks by others on grounds that the trust does not validly exist. Thus it will be necessary to ensure that the trust assets are properly identified and transferred to the trustee or brought under the trustee's control, and that the beneficiaries have been appropriately specified in the deed.

However, situations where we have seen potential and actual challenges to the validity of a trust centre concern certainty of intention and the capacity of the settlor:

(i) Certainty of intention

The settlor must form an intention to create a trust and to have transferred assets to the trustee to be held in accordance with the terms of the trust. It is important, therefore, that the settlor understands the terms of the trust and the legal ramifications of establishing it.

This is particularly important where the settlor is not from a common law jurisdiction but one that is subject to civil law or Sharia law and where English may not be the settlor's first language. Steps need to be taken to ensure that the settlor is independently represented by lawyers who not only understand trust law but can communicate with the settlor in his own language. Consideration should also be given to whether the deed should be translated into the settlor's own language to aid in understanding the English version which will eventually be executed.

Recently at the launch of RBC's trust company in Singapore, local lawyers commented that trust companies do not necessarily ensure that the settlor is independently advised but will simply have the settlor execute their standard deed. They do this on the back of conditions buried in their documentation that the settlor should take independent legal advice, but this is not necessarily emphasised. Without insisting on this, it seems that there is a risk of future attack on the basis that the settlor did not fully understand what he was doing and, therefore, did not form the requisite intent.

It is prudent, therefore, to ensure that the settlor is always independently advised.

(ii) Capacity

Lawyers representing the settlor will have a duty to ensure that he or she has the necessary capacity to create the trust. In most cases, this may be relatively straightforward. However, whenever there are concerns, or it is apparent that there may be subsequent challenges as to the settlor's capacity, it will be prudent to obtain legal and perhaps medical opinions at the time of the execution of the deed to support the fact that the settlor understood the terms of the trust and the ramifications of creating it. This was particularly important in one case that we handled where an attack on the grounds of undue influence and lack of capacity was anticipated and affidavits were taken from the settlor's lawyer and the doctors attending him. These were crucial in helping to deter the challenge that had been envisaged.

Perhaps the most important step to take is to ensure that the settlor is independently advised. That will usually prevent any claims that the trust is invalid on the grounds of lack of intention or lack of capacity.

(iii) An example: re Antle

This Canadian case from 2009 is a reminder of what can go wrong when the establishment of the trust is poorly implemented. The case involved Canadian tax planning which used a trust in

the jurisdiction of Barbados to take advantage of the Barbados/Canada tax treaty. Had the plan worked successfully, it would have eliminated Canadian tax on a capital gain that would have arisen on a planned arms length sale of shares of a Canadian company.

In short, the husband was to transfer his shares to the Barbadian trustee on a tax deferred basis and the Barbadian trustee was to later sell the shares to the wife at fair market value, thus triggering a gain in the Barbados trust. Had it worked, both those steps would have been free of Canadian tax. The wife was to then, shortly after receiving the shares, sell them to an arms length purchaser. The sale to the wife would have resulted in her owning the shares with a tax cost base equal to the proceeds of sale to the arms length third party.

The key to the strategy was that the gain on the sale of the shares was realised by the trust which then sought to rely on an exemption from Canadian capital gains tax under the Barbados/Canada tax treaty. However, the plan was poorly implemented. The trust deed and the directors' resolution effecting the transfer of the shares to the trust were both backdated. The trustees signed the documents to sell the shares in question to the wife before the settlor had executed the trust deed. The trust deed was apparently signed on the same date that the shares were sold to the arms length buyer when it should have been signed some time before that.

The tax court of Canada found that the trust was not valid for two reasons. Firstly, the husband lacked the required intention to form a trust and simply signed the requisite documents on the advice of his advisors, with the expectation that by doing so he would avoid tax in Canada. Secondly, the court held that the husband had not in fact transferred the shares to the trustee, as given the steps of the strategy he never intended to give up, or relinquish control of the shares or the money resulting from the sale. The Canadian tax court held therefore that the transactions were ineffective in that no trust was created.

b) Are the terms of the trust appropriate?

It is important that the trustees fully understand the settlor's intentions with respect to the establishment of the trust and that the trust deed has been drafted to achieve those intentions. For example, if there are certain types of assets which the settlor particularly wishes the trustee to hold (such as speculative investments or family company shareholdings) then plainly the trust deed needs to be drafted specifically to permit the holding and retention of such assets and the trustees powers drafted accordingly, giving them the flexibility to carry out the objectives of the trust. By the same token, there is clearly a risk that the use of a standard trust deed (which has not been tailored to the specific circumstances of the settlor) will not be fit for purpose.

Where the trust is being established and one of the objectives is tax planning, it is critical that proper tax advice is obtained and the terms of the trust are drafted to achieve the tax planning objectives. Furthermore, it is important to ensure that the terms of the trust deed are flexible enough that it can be adapted to address changes in family circumstances and legislation.

From a trustee's perspective, where the trustee is being asked to hold speculative assets or assume undue risk, it is not inappropriate for the trustee to mitigate these risks by inserting clauses exempting them from liability and such clauses should be considered when the trust is being drafted.

2) Investments

The global financial crisis has, of course, had an enormous impact on all manner of investments; trust portfolios have not been immune from these trends. Naturally enough, when markets are buoyant and investment performance is good, it may be tempting to pay less attention to the niceties of best practice. Of course this is a mistake because as markets have moved downwards some trustees and beneficiaries have seen marked falls in value and this in turn may throw light onto any weaknesses in process. Rightly or wrongly, that can be a hook upon which to hang criticism and can trigger disputes.

So what is best practice to avoid getting into disputes in this area? First, a trustee should ensure that he fully understands the investment powers provided to him.

How wide or narrow is the power that has been granted? We have seen situations in the offshore world where those responsible for administering the trust tend to treat each trust as having investment powers similar or identical to their standard trust deed and sometimes do not check whether the deed they are dealing with has been drafted differently.

The trustee should also understand the legal requirements or codes of practice applicable to the jurisdiction of the proper law of the trust.

For example, in the UK, under the terms of the Trustee Act 2000, a trustee will, of course, be required to establish a clear investment policy statement where they have authorized a person to exercise any of their investment management functions and for it to be reviewed on a regular basis and where necessary, updated. It is not unusual to find offshore trustees managing trusts which have been exported but which are still subject to English law and where perhaps investment policy statements have not been drawn up.

In most cases a professional investment manager will be required, and where an investment manager is appointed, then the trustee should record clear parameters and investment benchmarks and ensure an investment mandate and objectives are agreed. The choice of the most appropriate manager will depend on a variety of things such as the objectives of the trustee, the location of the beneficiaries, required income yields, the base currency and the time horizon for the investment of the trust assets. It is not appropriate, if the trustee is a bank owned trustee, simply to select the bank's own investment managers, without considering alternatives based on their experience, performance and price, since to do so is not a selection process at all.

The trustee also needs to ensure that the performance of the investment manager against the agreed performance benchmarks, and the mandate, are appropriately and independently monitored. It is not sufficient simply to rely upon the investment managers' own reports of their performance. Where there is poor performance over a period of time that cannot be adequately supported, then action needs to be taken to change the investment manager.

Particular attention is needed in two cases:

a) Characteristics of particular asset classes

Sometimes disputes arise in connection with the particular characteristics of specific classes of assets that a trust may hold. For example, there will often be wasting assets on a trust's balance sheet which are bound to fall rather than grow in value; the classic example would be a leasehold interest in real property. Another example would be those assets that have a capital value but do not generate income, for example, a collection of fine art. In both these cases, different beneficiaries will have different reactions to seeing these things in the trust accounts. An income beneficiary may not be pleased about non-income producing assets; a beneficiary with a prospective capital entitlement may be concerned about wasting assets.

In all these cases, assuming the trustee has acted within its powers in acquiring and retaining the assets, the key to avoiding disputes with unhappy beneficiaries is good communication from the outset and, of course, to make sure that one acts even-handedly (not necessarily equally) between them.

b) Family businesses

However, the most striking example of a difficult asset for a trustee is a private company shareholding, in particular a controlling shareholding in a trading business. The familiar scenario (which many practitioners will have encountered) is where the first generation - i.e. the settlor - has built up a business over a number of years as the product of his or her own entrepreneurial endeavour. Over time, as the settlor's children (the second generation) reach adulthood, one or more of them may follow in their parent's footsteps and enter the business full time. Another child may work in the business part time (for example someone who is at the same time caring for their own children, the third generation) and, of course, there may also be other children who are not involved and frankly not interested in the business at all.

The potential for disagreement here is obvious. There can be a falling out between settlor and trustee; between trustee and the various beneficiaries and between the different beneficiaries themselves. The dispute may be about the strategic direction of the company (e.g. aggressive growth requiring reinvested profits at the expense of dividends); it may be about the appropriate response to a take-over bid (a chance to exit the business and generate liquidity for the family or the abandonment of the settlor's

lifetime's endeavour?). There may also be disagreements about the extent to which the non-working beneficiaries benefit from the fruits of the working beneficiaries' labour.

Upon taking such a shareholding into trust, a trustee should of course look to see whether the trust instrument expressly dispenses with the normal duty to diversify investments and/or gives a power or a direction to refrain from disposing of these shares. This at least may be the answer to those beneficiaries who would prefer the trustees just to sell up and realize some capital.

As to the unequal contributions of different beneficiaries, there may be solutions outside of the trust. This takes us beyond the scope of this article but, by way of illustration, a beneficiary who does not have the skills to contribute to the family business may be able to make an impact elsewhere, for example, by taking a lead with the family's philanthropy and chairing the board of a grant-making charity.

Overall, there is no single answer (and no easy answer) to some of these family business tensions. The way to minimize disputes is not only good communication but also to "know your client" deeply and to have good, regular dialogue with the family; spotting and addressing these issues before they develop into something tougher to resolve.

3) Administration

Many issues arising from the administration of the trust or as to the fairness of the trustee's decisions as between beneficiaries can be avoided altogether or mitigated by good practice in the ongoing running of the trust.

a) Regular contact with the beneficiaries

It is critical that the trustees meet with the beneficiaries of the trust at the outset and on a regular basis to ensure that they understand the provisions of the trust deed and what is happening with respect to the administration of the trust. It is also important to understand each beneficiary's situation, goals, needs and aspirations in order that the trustee can exercise its discretionary powers effectively.

By keeping close to the beneficiaries and building a strong relationship, the trustee is more likely to identify from the outset when things are starting to go wrong or when there are concerns being raised either about the administration or with respect to potential disputes among the beneficiaries. Identifying such concerns early allows the trustee to clarify any misunderstandings before they fester and become bigger issues.

It is also very beneficial to bring the next generation into the discussion. We have seen a number of trusts where the settlor, who was the wealth creator and possibly a dominant individual, is the sole point of contact with the trustees and, when he dies, the next generation, who may not even have been aware of the existence of the trust, are deeply suspicious of what the trustees have been up to. They will commonly scrutinize the investment performance of the trust (the investment policy no doubt having been heavily influenced by the settlor) and seek to blame the trustees for any poor performance. In contrast, where the next generation are brought into a dialogue with the trustees during the settlor's lifetime and understand the investment process, they are far less likely to seek to blame the trustees for poor investment performance. It also means that on the settlor's death, there is an easy transition from one generation to the next.

At a minimum, annual trustee meetings should be held with the beneficiaries (and where appropriate their own advisors) to include presentations from investment managers or other advisors to the trustees. More frequent meetings should be held where, for example, the size or complexity of the trust assets warrants it.

In our experience, the closer the relationship with the beneficiaries, the more forgiving they are likely to be when something does go wrong.

b) Letter of wishes

The settlor's letter of wishes should be updated regularly to ensure that it captures any changes in circumstances in the family or the intentions of the settlor.

c) Maintaining good records

The trustees also need to ensure that they maintain comprehensive books and records.

(i) Minute books

These should include clear and accurate records evidencing the decisions taken by the trustee (or of the directors of underlying companies owned by the trust

where the trust company may also be providing directors).

(ii) Correspondence files

Correspondence files, whether in paper form or held electronically, should also be comprehensive and support the fact that the trustee has gathered the appropriate information, and where necessary, advice regarding decisions that are being taken and that if called upon can demonstrate the fact that such decisions are being appropriately taken in the jurisdiction in which the trust is resident.

The file should reflect the fact that the trustee has not only considered all relevant facts and obtained all necessary information but that this has been achieved in a time scale that allows for a considered decision.

We came across one example on a file which we inherited from another trustee in which an offer to purchase a significant piece of UK real estate was presented by a beneficiary at say 12 noon with fairly scant background information. In an effort to demonstrate what were perceived to be good client service skills, the trustee promptly sent a response at 12.05, accepting the offer. Such actions, although perceived to be helpful, naturally leave open the argument that the trust is really being run by the beneficiaries not the trustees.

Re Garron was another Canadian tax case where, as with re Antle, there had been an attempt to take advantage of the Canadian/Barbados tax treaty to shelter capital gains arising on the sale of shares of a Canadian company.

The gain was disallowed by the Canadian tax authorities because they found that the trust was not being "centrally managed and controlled" in Barbados but was actually being managed and controlled by the beneficiaries resident in Canada; hence the trust was resident in Canada. The gain that was disallowed treatment under the treaty was over C$450 million and the resulting tax payable was approximately C$133 million.

Trustees should ensure that their correspondence files do not contain a flow of correspondence from the beneficiary(ies) providing instructions to the trustee, for example, as to where to pay funds or which assets to buy or sell. It is files of this nature which will make it easier for those wishing to attack the trust to demonstrate that the trustees are mere puppets and not really exercising independent management and control. Where this behaviour emerges in the trust administration, it is important to educate the beneficiary(ies) about the role of the trustee and the importance of maintaining the integrity of the structure.

Correspondence files should also be professional in terms of content. A good rule of thumb is never commit anything to writing that you would not want read out in Court.

(iii) Accounts

It is also important that proper trust accounts are prepared on an annual basis and sent to all primary beneficiaries to apprise them of the position of the trust administration. Depending on the assets held, more frequent reporting should be sent to apprise the beneficiaries of the position especially with respect to investment portfolios held. Such ongoing reporting will help to prevent any misunderstanding arising with the beneficiaries regarding the management of the assets.

4) Training

Clearly, it is critical that trust staff are properly trained and kept up-to-date with changes to legal and tax matters in the major markets in which they operate.

Ideally staff should be required to obtain appropriate qualifications such as STEP, legal or accountancy qualifications but this needs to be augmented by in-house programmes. It is useful to have legal or tax specialists present to trust staff on topical matters from time to time but especially when there are major changes to case law or legislation which affects trust administration.

Tact, diplomacy and the ability to reduce the temperature of a dispute are also vital skills if disputes are to be well handled when they do arise. By contrast,

a simple enquiry from a beneficiary (for example, about something in the accounts which needs clarifying) can be unnecessarily escalated into an argument if the response from the trustee is insufficient or unnecessarily hostile, self-defensive or inflammatory.

5) Internal procedures

It is generally useful for staff of trust companies to be able to refer an issue where there is a dispute or a risk of litigation to an internal committee made up of senior staff who are experienced in dealing with such matters. This assists in ensuring that matters are dealt with in the most effective manner, working closely of course with external legal advisors. We have two such committees within the RBC trust group, one which is focused on our business in the Channel Islands and one larger body available to our global trust group.

6) Fees

This is not the time or place for a detailed examination of charging practices but one can hardly address the topic of disputes in the context of professionally administered trusts without at least briefly mentioning fees. There is, of course, a wide range of charging practices across the trust world: fixed fees, hourly rates and time-based charging, ad valorem fees, relationship pricing etc. We all also face conflicting pressures on charges both downward and upward: downward pressure to quote for new business at a rate which we hope will be attractive in a competitive market and upwards because to be an excellent fiduciary and to be reasonably rewarded for that is the essence of our business.

In our experience, the golden rule to minimize fee disputes is to avoid surprises. As far as possible, be clear and be upfront about charges; explain the circumstances in which fees may change and work on the basis of clear, up-to-date, explicitly communicated terms of business and send bills regularly (at least quarterly) to avoid a build up of fees which might provoke a strong reaction from the beneficiaries.

When disputes arise

Sometimes no matter how thorough the administration and how good the communication with the beneficiaries, disputes will arise. All trust practitioners will be familiar with the famous Alhamrani litigation which kept the Jersey courts busy for 6 years, ran to more than 100 separate hearings and involved so many lawyers that the main hearing had to be relocated to a hotel.

1. Understand the precise nature and extent of the problem

Fortunately not many disputes are quite as complicated as Alhamrani but, even so, when disputes do arise it is helpful to ask some basic questions in order to clarify what legal advice is going to be required and to ascertain how matters should be handled:-

(a) Who is the dispute between?

(b) What is the dispute about?

(c) What impact, if any, will the dispute have on the administration of the trust?

(d) Is the subject matter of the dispute a matter affecting the trust, or is it a personal matter between the parties?

(e) What are the duties of the trustee?

(f) Is the trustee placed in any position of conflict?

(g) What are the cost implications of the dispute?

2. Taking legal advice

In seeking legal advice as trustee where the dispute involves a potential claim from a beneficiary alleging breach of trust, it is critical that the lawyer representing the trustee is able to take a practical and measured approach in dealing with the allegation and in advising how to proceed. In our experience, a constructive approach aimed at resolving the dispute satisfactorily as early as possible is most likely to bear fruit. By contrast, a more aggressive approach carries the risk of inflaming the situation.

We have seen situations where a strong and aggressive response to lawyers acting for the beneficiary simply served to exacerbate matters. Within a very short period of time in that case, both sides were at loggerheads and moving swiftly towards litigation instead of resolution.

It is worth noting that legal advice taken at the cost of the trust fund is potentially disclosable to the beneficiaries.

3. Litigation cost implications and the position of the trustee

In analyzing the cost implications of the dispute and the position that the trustee should adopt, it is instructive to have regard to the categorization of disputes by Mr Justice Lightman in the English case of Alsop Wilkinson v

Neary. In that case the judge identified three main types of trust action; trust disputes, beneficiary disputes and third party disputes. Let us remind ourselves of these categories:

a) Trust disputes

Mr Justice Lightman sub-divided trust disputes into:-

- Friendly litigation, and
- Hostile litigation

Friendly litigation involves issues brought before the Court by the trustees regarding, for example, the construction of trust documents regarding an ambiguous provision or where guidance is sought from the Court concerning some difficulty in the administration.

In such cases, generally, the costs of all parties are considered to be necessarily incurred for the benefit of the trust fund. Hence, in these friendly disputes the general position is that, provided the trustee has acted impartially as between the beneficiaries, they will be entitled to their reasonable costs from the trust fund.

Hostile litigation will generally relate to an attack on the validity of the trust or a dispute relating to beneficial interests. These claims may be brought by various parties including trustees in bankruptcy, creditors or others in which case it may be unclear on whose behalf the trustee is actually holding the assets.

In such circumstances, the law is clear that the trustee's duty is to remain neutral. The trustee should allow the parties to fight the matter out between them and to provide the Court with whatever information it needs in arriving at its decision.

Provided the trustee does no more than adopt a neutral position, it is not necessary to obtain prior authorization of the Court regarding its costs in the form of a Beddoe order.

b) Beneficiary disputes

These generally involve a dispute with one or more of the beneficiaries as to the propriety of any action taken (or omitted to be taken) by the trustees. This may lead to proceedings by a beneficiary alleging breach of trust or seeking the removal of the trustees and/or damages for the alleged breach.

A beneficiary dispute is regarded as ordinary hostile litigation in which costs follow the event.

c) Third party disputes

This is generally a dispute with persons, other than beneficiaries, in respect of other rights and liabilities, for example in contract or tort, assumed by the trustee in the course of the administration of the trust.

In these cases, trustees are generally entitled to an indemnity for reasonable expenses incurred in properly bringing or defending an action for the benefit of the trust fund. Views may vary as to whether proceedings are properly brought or defended and so, to avoid the risk of a challenge to their entitlement to an indemnity, trustees are well advised to seek Court authorization before they proceed.

For present purposes, we will not devote further attention to friendly disputes or third party disputes but will look in more detail at hostile actions and beneficiary disputes.

4. Hostile disputes

As outlined above, hostile disputes are a subset of 'trust disputes' in Mr Justice Lightman's classification and they will usually involve matters such as an attack on the validity of the trust or a dispute surrounding the beneficial interests.

A typical scenario might involve a family at war with itself. Perhaps a dispute between siblings once the settlor (and patriarch of the family) has died or where the settlor has remarried and the new spouse is both unpopular and perceived to be benefitting from the trust at the expense of other family members.

These situations create all sorts of headaches for the trustee, not least because the trustee often gets caught in some fairly intense crossfire and any decisions of the trustee which, in the mind of the aggrieved beneficiary, appear to favour one beneficiary over another, invariably become the focus of intense criticism.

In such situations the trustee needs to be able to demonstrate that it has properly exercised any discretion and that it is acting fairly and neutrally between the beneficiaries.

In any hostile dispute as to the validity of the trust or a dispute surrounding the beneficial interests, the duty of the trustee is generally to remain neutral. However, as long as the trustee

remains neutral, it is not unreasonable to try to steer a course away from litigation which will inevitably be costly and divisive.

In this regard, the relationship built up with the beneficiaries over the years can be very powerful in trying to resolve the position. The trustee should try to be alive to any early signs of a dispute and try to deal with it at that stage. Sometimes a protector can be a useful source of information as to how to deal with the aggrieved beneficiary.

Up-to-date letters of wishes can be very useful in satisfying the beneficiary that the trustee is acting with due regard to the stated wishes of the settlor, especially where there are changes in family circumstances such as remarriages or bereavements.

Accurate records can also assist aggrieved beneficiaries to assess their position. We have seen disputes arise as a result of a misunderstanding or inaccurate recollection of events: sometimes these things can be quickly clarified, provided the trustee has good historical records over the lifetime of the trust.

In some cases it may be appropriate to suggest that the beneficiaries in dispute with one another seek to address the matter via mediation rather than pursuing costly and divisive litigation. Mediation can be beneficial because it is voluntary, confidential as a mediator is independent, the process is less formal than court proceedings and, of course, because generally mediation will be less costly than traditional litigation.

5. Beneficiary disputes

As explained above, a beneficiary dispute as categorized by Mr Justice Lightman is one where one or more of the beneficiaries is seeking to challenge an action taken by the trustee or omitted to have been taken by the trustee. This may lead to proceedings alleging breach of trust and/or seeking the removal of the trustees.

Once again, comprehensive and accurate records together with solid administrative practices will hopefully provide a defence to any such claims but the trustee will no doubt need legal advice as to the most appropriate response to such allegations.

Initially it may be best (if the allegation is coming directly from a beneficiary or beneficiaries) for the trustee to take legal advice but then to respond directly to the beneficiary in the hope of resolving matters in that way. Where the trustee believes that the allegations are without foundation then naturally it will want to defend its position firmly but all the time with a view to bringing matters to an early resolution.

In those cases where the trustee has indeed made a mistake or error to the detriment of the trust, an offer to settle should be made swiftly to remedy the position.

6. Disclosure

Sometimes the trustee may be asked by a beneficiary to disclose information and documents against the background of a dispute. This has always been a thorny issue and again the trustee should seek legal advice about what should and should not be disclosed.

The main principles are that a beneficiary is generally entitled to see trust documents. By contrast, beneficiaries do not have the right to force trustees to explain their discretionary decisions.

These include:-

(i) Deliberations as to how a trustee should exercise his functions as a trustee;
(ii) The reasons for any decision made in the exercise of those functions;
(iii) Any material upon which a decision was or might have been based.

These principles were first laid out in re Londonderry's Settlement and are contained in Guernsey Trust Law 2007.

The topic of the disclosure of trust documents (and of what counts as a trust document) is beyond the scope of this paper. Practitioners will be familiar with the case of Schmidt v Rosewood Trust which approached the matter on the basis that the right to seek disclosure of documents was a proprietary right and one aspect of the Court's inherent jurisdiction to supervise and intervene if necessary in the administration of a trust.

An interesting example arose in M & L Trustees (2003) JRC 002A, a Jersey case. The Royal Court did not allow a spouse of the settlor who was seeking disclosure under the trust while at the same time attacking the integrity of the trust, to claim rights arising from her status as a beneficiary under the

trust and at the same time deny that status. Her request for disclosure would be viewed sympathetically once the attack on the trust had been dropped.

7. **Alternatives to litigation – the Guernsey experience**

Another course of action to consider is the use of alternative dispute resolution ("ADR"). Courts are always keen for people to explore ways of solving their disputes other than by formal proceedings. Where a dispute has gone beyond the stage at which the parties are able to solve it themselves, ADR is increasingly popular as an alternative to litigation, not least because it can be quicker, cheaper, more private and much less stressful. By way of illustration, Guernsey has taken an interesting step in encouraging ADR with specific provisions in the Guernsey Trust Law of 2007. These rules provide for resolution of claims against a trustee founded on breach of trust through ADR without court intervention where all parties, including minors and unborns, are properly represented.

ADR in the context of this Guernsey Law is defined to include "conciliation, mediation, early mutual evaluation, adjudication, expert determination and arbitration". Conciliation and mediation each involve the intervention of a third party whose function it is to assist the parties in dispute to reach agreement. No judgment or outcome is forced upon them and any agreement reached will, by definition, be freely reached by the parties. It is rare that both parties will be completely satisfied with the outcome but that outcome, once agreed, will of necessity be one with which both parties can live. Early mutual evaluation involves an independent party examining the issues from all sides and providing the disputing parties with an indication of how he or she thinks proceedings, if they were ever started in Court, would end. Retired judges are often used in this context. This evaluation is then digested by the parties who will either accept the findings or perhaps use them as a basis to resolve the dispute between themselves without too much further argument.

Adjudication, expert determination and arbitration are more akin to Court proceedings in that, effectively, a case is presented and defended and the adjudicator, the expert or the arbitrator will pronounce a judgment. The degree to which that judgment is binding will largely depend upon the intentions of the parties but an arbitration conducted under the auspices of arbitration legislation would, by law, be binding. Dissatisfaction with the arbitrator's judgment could, in certain circumstances, lead to an appeal to a Court.

This Guernsey law enables ADR proceedings to be commenced without reference to a Court if the terms of the trust so direct or authorise and thus it would be helpful for a trust instrument to contain one or more of those provisions. However, if there is no reference to ADR in the trust instrument, all is not lost: the Court can order a breach of trust claim against the trustee to be referred to ADR in any event.

Where such a dispute arises, proceeds to ADR and the dispute is then settled in the course of ADR proceedings, subject to what is said below, that settlement is binding on all the beneficiaries of the trust (including beneficiaries not yet in existence, minor beneficiaries and beneficiaries under a legal disability).

For that settlement to be binding, the beneficiaries must all be represented in the ADR proceedings. A beneficiary can appear in person (or by his guardian if a minor or a person under legal disability) or as a member of a class. If he is not to be present or represented at the ADR proceedings, he must have had notice of them and to have been given a reasonable opportunity of being heard. Regardless of whether the ADR was instigated in accordance with the terms of the trust or by a court order, if the beneficiary concerned is either not yet ascertained, in existence, is a minor or a person under legal disability then that particular beneficiary must be independently represented by a person appointed for the purpose by a court.

In summary, it is now clear that ADR can play a role in solving trust disputes where there is an allegation of breach of trust but only if ADR is authorised or required by the trust instrument and if all the beneficiaries are of full age, ascertained and not under a legal disability can the procedure be carried out without reference to a Court. If the trust instrument does not direct or authorize ADR and/or if within the class of beneficiaries there are unascertained, minor or unborn

beneficiaries or beneficiaries with a legal disability, then the intervention of the Court will be necessary but only to either sanction ADR if the trust instrument does not direct or authorise it or to appoint someone to represent unascertained minor or unborn beneficiaries or beneficiaries with legal disability. It is highly likely however that any Court would be supportive of a means of solving a dispute which does not involve Court time.

Finally, bear in mind that these procedures are there to give trustees protection if ADR methods are used to solve trust disputes involving allegations of breach of trust by the trustees. In the case of disputes between beneficiaries (or perhaps between beneficiaries and trustees) as to, for example, their wishes for the future direction of the trust, and where the trustees are not being criticized but are looking for help to break an impasse, ADR of the consensual variety involving an independent mediator or conciliator could be a useful way forward.

If all else fails, what about trustee exoneration clauses?

It is a truism to say that the role of trustee is one which carries onerous responsibility. No trustee can get everything right all of the time and, of course, it has become standard practice for trustees to limit their liability expressly to mitigate their risks.

English statute law itself allows certain protection, for example for retiring trustees, but trust instruments commonly go further and include wide, express limitations of potential liability for everything except actual dishonesty or fraud. This is not an uncontroversial topic. A layman might ask us or any trustee who is acting for reward: if I am paying you for this service, why can I not look to you to make amends if things go wrong on your watch? And indeed the subject has been examined in some detail in England by the Law Commission (consultation paper in 2003 followed by a report in 2006) and by STEP which produced its own practice rule in response to that report.

It is absolutely clear that as a matter of English Law, trustees are allowed to exclude liability for negligence. This was restated by the Privy Council recently in the Guernsey case Spread Trustees v Hutcheson upholding the Court of Appeal in Armitage v Nurse .

So what is the answer to the layman who is surprised that a trustee wants to rely on a wide exoneration clause? STEP's practice rule requires that where liability for negligence is to be excluded this exclusion is notified to the settlor and the settlor gives "full and informed acceptance". So at least the settlor will have known what he is agreeing to. But of course, the settlor may be deceased at the time of the default and, in any event, it is the beneficiaries who will bear the loss, not the settlor.

Our view as professional trustees is if there has been a mistake – our mistake - we will generally be reluctant to hide behind an exclusion clause because that runs completely counter to the whole thrust of the fiduciary integrity we espouse. This will be largely based on the merits of the claim or allegations against us and we may take a different view if the claims or allegations are without merit.

Conclusion

The role of the modern trustee is, by its very nature, a complex one and there will always be a great deal of scope for contentious issues to arise in particular where discretionary powers are exercised and where difficult assets are held and for as long as families members continue to fall out with each other.

Best practice in trust creation and administration will minimize the occasions of dispute. However, when problems do arise, good advice, a cool head and the right approach to solving the dispute can prevent any of these contentious issues of modern trusteeship from turning into full blown litigation.

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